Report to those charged with governance (ISA 260) 2014/15

Surrey Heath Borough Council

31 March 2016

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The contacts at KPMG in connection with this report are:

Neil Hewitson
Director
KPMG LLP (UK)

Tel: 0207 311 1791
neil.hewitson@kpmg.co.uk

Charlotte Goodrich
Manager
KPMG LLP (UK)

Tel: 0207 311 2181
charlotte.goodrich@kpmg.co.uk

Tanny Datta
Assistant Manager
KPMG LLP (UK)

Tel: 0207 311 4495
tanny.datta@kpmg.co.uk

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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. The Audit Commission issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

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Introduction

This document summarises:

- **The key issues identified during our audit of the financial statements for the year ended 31 March 2015 for the Authority; and**
- **Our assessment of the Authority's arrangements to secure value for money.**

Scope of this report

This report summarises the key findings arising from:

- our audit work at Surrey Heath Borough Council ('the Authority') in relation to the Authority's 2014/15 financial statements; and
- the work to support our 2014/15 conclusion on the Authority's arrangements to secure economy, efficiency and effectiveness in its use of resources ('VFM conclusion').

Financial statements

Our *External Audit Plan 2014/15*, issued in March 2015, set out the four stages of our financial statements audit process.

This report focuses on the third stage of the process: substantive procedures. Our on site work for this took place principally in July and August 2015, and then in December 2015 – February 2016.

We are now in the final phase of the audit, the completion stage. Aspects of this stage are discharged through this report.

VFM conclusion

Our *External Audit Plan 2014/15* explained our risk-based approach to VFM work. We have now completed the work to support our 2014/15 VFM conclusion. This included:

- assessing the potential VFM risks and identifying the residual audit risks for our VFM conclusion; and
- considering results of relevant work by the Authority and other inspectorates and review agencies in relation to these risk areas.

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages;
- Section 3 sets out our key findings from our audit work in relation to the 2014/15 financial statements of the Authority; and
- Section 4 outlines our key findings from our work on the VFM conclusion.

Our recommendations are included in Appendix 1. We have also reviewed your progress in implementing prior recommendations and this is detailed in Appendix 2. The detailed listing of audit adjustments is included in Appendix 3.

Acknowledgements

We thank officers and Members for their continuing help and cooperation throughout our audit work.

Headlines

This table summarises the headline messages for the Authority. The remainder of this report provides further details on each area.

Context to the 2014/15 external audit	2014/15 has been a challenging year for the Authority's finance team. A new Civica ledger was implemented on 1 April 2014. There have been significant difficulties and delays with the implementation and establishing a 'business as usual' state. The introduction of the new ledger created additional resourcing pressures on the finance team. These challenges are in part reflected in the timeliness and quality of the Authority's draft 2014/15 financial statements. The Authority submitted its draft financial statements for audit on 8 July 2015, missing the submission deadline of 30 June 2015. In addition, the Authority submitted its draft Whole of Government Accounts ("WGA") pack on 29 July 2015, missing the Department of Communities and Local Government ("DCLG") deadline of 10 July 2015. The Authority was unable to provide sufficient supporting evidence for material balances within the financial statements, before the 30 September DCLG accounts audit submission deadline. As a result, the Authority missed this deadline. Subsequent to this, the Authority also missed the WGA submission deadline on 2 October 2015. We have identified a higher number of errors in the accounts than in previous years. A key contributor to this was the reduced level and robustness of quality assurance over the draft financial statements.
Financial statements proposed audit opinion	We anticipate issuing an unqualified audit opinion on the Authority's financial statements by 31 March 2016. We will also report that the Annual Governance Statement complies with guidance issued by CIPFA / SOLACE in June 2007. This is review and satisfactory conclusion of testing over the MiRS, Cashflow Statement and supporting notes to the accounts, and subject to completion of our final quality and review procedures.
Audit adjustments	Our audit identified a total of 41 significant audit adjustments, of which 20 are material, covering both ledger and disclosure amendments. Of these 41 adjustments, 20 impact on the prime financial statements. The net impact of these on the financial statements is: ▪ General Fund: £1,058k decrease ▪ Surplus on the provision of services: £166k increase We have included a full list of significant audit adjustments at Appendix 3. The majority of these have been adjusted by the Authority. There are two unadjusted errors, we are satisfied these are immaterial to the financial statements. We have raised recommendations in relation to the matters highlighted above, which are summarised in Appendix 1.
Accounts production and audit process	The Authority's process for the production of the 2014/15 financial statements was not as strong as in previous years, as evidenced by the considerably higher volume of errors. Working papers produced by the finance team to support the draft accounts were not of sufficient quality to support the balances and disclosures made in the draft accounts and were not made available in a timely fashion. As a result our work was not completed within the original agreed timescales. Given the challenges faced we are required to submit a fee variation request to the Public Sector Audit Appointments Limited ("PSAA") to cover the additional costs of undertaking this year's audit. We have raised a high priority recommendation regarding implementing a more robust quality assurance process over the production of the financial statements, full details are included within Appendix 1.

Headlines

Key financial statements audit risks	We review risks to the financial statements on an ongoing basis. We identified three financial statement audit risks in our 2014/15 external audit plan: ▪ Management override of controls: 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 due to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We have not identified any specific additional risks of management override relating to this audit. ▪ The Authority implemented a new Civica general ledger system on 1 April 2014, during which existing balances were transferred from the old Oracle system to the new Civica system. There is a risk therefore that information has not been migrated over accurately or completely, which could result in the misstatement of opening balances. ▪ Valuation of land and buildings: This was because of the materiality of the value and the judgment involved in determining the carrying amounts of property assets. In addition, auditing standards require us to make a rebuttable presumption of a risk of fraudulent revenue recognition. We do not consider this to be a significant risk for local authorities as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebut this risk and do not incorporate specific work into our audit plan in this area over and above our standard fraud procedures. However we keep our rebuttal of this risk under review throughout the audit. We have worked with officers throughout the year to discuss this key risk and our detailed findings are reported in section 3 of this report. Matters arising from this work are reported in Appendix 1.

Headlines

Control environment	We have reviewed the overarching key controls the Authority has in place over budget monitoring, bank reconciliations and journals amendments. Our audit identified the following discrepancies: ▪ Budget monitoring: The Authority was not able to profile its budgeted expenditure correctly using the new Civica ledger system in 2014/15. As a result, the Authority was unable to undertake monitoring of budget vs actuals in year. Instead, the Authority undertook monitoring of service level actuals vs year end forecast outturn. This type of budget monitoring had been undertaken in prior years, and we have previously recommended this monitoring be undertaken on a real time actuals basis. ▪ Bank reconciliations: The Authority was unable to produce a monthly bank reconciliation until February 2015, as the new bank reconciliation module of the Civica ledger could not be correctly applied. However, this bank reconciliation did not agree to underlying records and did not appropriately reconcile the bank account balance to the general ledger. The Authority undertook a year end exercise to prepare the year end bank reconciliation in June 2015, and this has been found to appropriately reconcile the bank to the ledger. This fundamental control did not operate effectively during 2014/15. ▪ Journals authorisation: The Authority has a two stage journals authorisation process in place; all journals are required to be authorised by an officer separate to the preparer. All journals over £20k are required to be second authorised by the Head of Finance. Our detailed testing found that out of 18 journals over £20k tested, 7 had not been second authorised. We are satisfied that effective segregation of duties is in place, however note that the Authority's own internal policy has not been adhered to in these cases. ▪ The draft financial statements submitted for audit required a significant number of material amendments, and working papers were not always of appropriate quality for audit purposes. This indicates a breakdown in the quality of the accounts production process and highlights concerns over the overall control environment. The implementation of the new Civica general ledger system during 2014/15 has contributed to this overall weakening of arrangements, due to the additional pressure on staff time. ▪ Our audit work identified discrepancies between the opening trial balance per the new Civica ledger system and the prior year audited financial statements. These discrepancies were initially identified by an external consultant at the beginning of the year, however amendments were not made. As such corrections were identified and required during our audit, despite assurance work having been carried out in this area by an independent consultant. ▪ Our sample testing of cut-off controls and non-pay expenditure within the Comprehensive Income and Expenditure Statement ("CIES") identified three transactions totalling £260k which had been included in the incorrect year. We have previously raised recommendations regarding the cut off of transactions where transactions were identified as having been recorded in the incorrect accounting period. We undertook significant additional testing and from this are satisfied that we have materially quantified the extent of errors. The Authority has amended these items. *Continued overleaf*

Control environment (cont.)	▪ Testing of Property, Plant and Equipment ("PPE") and Investment Properties, identified that the Authority had not undertaken an exercise to satisfy itself that the fair value of assets valued at 1 April 2014 was not materially different to their carrying values as at 31 March 2015. This is required by the Code of Practice on Local Authority Accounting. The Authority engaged its external valuer to provide this review during the audit, which resulted in a further revaluation increase of £1.4m. As a result of the above items we have raised a total of ten recommendations in response to each of these items, of which six are high priority. Full details of these items are given in Appendix 1.
Completion	At the date of this report our audit of the financial statements is substantially complete, except for completion procedures and testing over the Whole of Government Accounts ("WGA") submission. Before we can issue our opinion we require a signed management representation letter. We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.

Headlines

VFM conclusion and risk areas	We consider two criteria in determining our Value for Money conclusion as specified by the Audit Commission: arrangements to secure financial resilience; and arrangements to secure economy, efficiency and effectiveness. Within these two criteria there are 64 risk triggers specified by the Audit Commission, for which we review the Authority's arrangements and consider if they indicate an increased risk requiring additional audit attention. Two of these risk triggers are lack of capacity within the finance team, and poor management of capital projects. As a result of matters identified throughout the year, we identified these items as significant risks to the Value for Money conclusion, and undertook additional audit procedures as appropriate. **Inconsistent application of core elements of the financial control environment** The Authority faced a number of challenges following the introduction of a new financial ledger system on 1 April 2014. It had a detrimental impact on the consistency with which fundamental financial controls were applied in year. For example, no bank reconciliations were performed during 2014/15 and there were significant delays in the preparation of the year-end bank reconciliation as at 31 March 2015. The ledger implementation also meant that the regular monitoring of actual expenditure against budgets did not take place during 2014/15. **Capacity, capability and structure of the finance function** The draft financial statements were submitted late on 8 July 2015, missing the DCLG submission deadline of 30 June 2015. In addition, the WGA DCT pack was submitted late on 29 July 2015, missing the DCLG submission deadline of 10 July 2015. The draft accounts submitted for audit contained a large volume of significant audit adjustments, and the primary statements did not reconcile to one another. During the audit process, audit working papers were not always of appropriate quality to support accounts disclosures and there were delays in receiving key working papers and evidence, which delayed the audit process. External consultants were required to review and revise certain accounts figures from those presented in the draft financial statements. The Authority was unable to provide sufficient supporting evidence for material balances within the financial statements, before the 30 September DCLG accounts audit submission deadline, or the 2 October WGA submission deadline. As a result, the Authority missed these deadlines. There was not an appropriate level of quality control review of the draft financial statements and there was not an appropriate plan in place to ensure that the finance team structure and resources could be utilised effectively to meet statutory responsibilities. These capacity and capability issues are compounded by pressures within the resource model of the finance function, the structure of which is under review. On this basis we cannot satisfy ourselves that the capacity of its finance team in 2014/15 were sufficiently robust to ensure financial control, or to ensure efficiency and productivity. In light of the above we have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources and to ensure financial resilience in 2014/15, except for in regard to the capacity of the finance team. We anticipate issuing a qualified (except for) VFM conclusion by 31 March 2016. Further details are given in section four.

Headlines

Public Interest Reporting (not discussed further in this document)	In auditing the accounts we must consider: ■ whether, in the public interest, we should make a report on any matter coming to our notice in the course of the audit, in order for it to be considered by Authority 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 the conclusion of our audit. There are no matters in the public interest that we wish to raise at this time.

Financial Statements: proposed opinion and audit differences

We anticipate issuing an unqualified audit opinion in relation to the Authority's financial statements by 31 March 2016.

The wording of your Annual Governance Statement complies with guidance issued by CIPFA / SOLACE in June 2007.

Our audit has identified a total of 41 significant audit adjustments.

Proposed audit opinion

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority's financial statements following approval of the Statement of Accounts by the Performance and Audit and Standards Committee on 31 March 2016.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. There are no uncorrected audit differences.

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 level for this year's audit was set at £450k. See Appendix 5 for more information on materiality. Audit differences below £45k are not considered significant.

Our audit identified a total of 41 significant audit adjustments, which we set out in Appendix 3. The most significant of these are summarised below. It is our understanding that these will be adjusted in the final version of the financial statements and we will confirm that they have been processed before issuing our audit opinion.

Of the audit adjustments we have identified, 20 impact on the prime financial statements. For example:

- Reduction of an impairment charge made to the CIES by £1,412k, increasing the surplus by this amount.
- Misclassification of several investments items within the Balance Sheet between Short-term and Long-term Investments, amounting to £9,624k in total.
- Adjustment of £283k of income from Housing Services to Adult Social Care within the CIES.
- Inclusion of £420k in additional expenditure and removal of £246k in income within Central Services to the Public in the CIES.
- Reclassification of £876k from expenditure to income for Cultural, Environmental and Planning Services.
- Movement of £8,123k from Available for Sale Financial Assets in current investments to long-term investments within Note 34.

In addition we identified presentational adjustments required to ensure that the accounts are compliant with the *Code of Practice on Local Authority Accounting in the United Kingdom 2014/15 ('the Code')*. We understand that the Authority will be addressing all of these.

Annual Governance Statement

We have reviewed the Annual Governance Statement and confirmed that:

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

Financial Statements: proposed opinion and audit differences

Our audit has identified a total of 41 significant audit adjustments. Of these, all are material to the financial statements and 20 impact on the prime financial statements.

The impact of these adjustments is to:

- **Decrease the balance on the general fund at 31 March 2015 by £1,058k; and**
- **Increase the surplus on the provision of services for the year by £166k.**

Comprehensive Income and Expenditure Statement for Year Ending 31 March 2015

£'000	Pre-Audit Expenditure	Post-Audit Expenditure	Pre-Audit Income	Post-Audit Income	Pre-Audit Net	Post-Audit Net	Audit Adjustment
Central services to the public	1,516	1,936	(622)	(868)	894	1,068	174
Cultural, environmental & planning services	11,621	9,822	(5,861)	(5,160)	5,760	4,662	(1,098)
Highways, roads & transportation	1,480	1,480	(2,569)	(2,569)	(1,089)	(1,089)	0
Housing services	19,596	19,596	(17,527)	(17,244)	2,069	2,352	283
Adult social care services	2,315	2,315	(1,330)	(1,613)	985	702	(283)
Corporate & democratic core	2,335	2,429	(42)	(42)	2,293	2,387	94
Non distributed costs	0	0	0	0	0	0	0
Other operating income and expenditure	0	0	0	0	0	0	0
Cost of services	**38,863**	**37,578**	**(27,951)**	**(27,496)**	**10,912**	**10,082**	**(830)**
Other operating expenditure							
Parish precepts					509	509	0
Payments to Government housing capital receipts pool					0	0	0
					509	**509**	**0**
Financing and Investment Income and Expenditure							
Pensions interest cost and expected return on pensions assets					1,348	1,348	0
Interest receivable and similar income					(241)	(241)	0
Income and expenditure in relation to investment properties and change in their fair value					(2,459)	(2,633)	(174)
					(1,352)	**(1,526)**	**(174)**
(Surplus) or deficit on discontinued operations					**0**	**0**	**0**
Taxation and non-specific grant income							
Council tax income					(7,756)	(7,756)	0
Non domestic rates					(1,990)	(1,152)	838
Non-ringfenced government grants					(2,591)	(2,591)	0
Capital grants and contributions					(283)	(283)	0
					(12,620)	**(11,782)**	**838**
(Surplus)/deficit on provision of services					**(2,551)**	**(2,717)**	**(166)**
(Surplus) or deficit on revaluation of PPE					(9,328)	(9,251)	77
Actuarial (gains)/losses on pension assets/ liabilities					5,699	5,699	0
(Surplus) or deficit on revaluation of available for sale financial assets						(144)	(144)
Other comprehensive income and expenditure					**(3,629)**	**(3,696)**	**(67)**
Total comprehensive income and expenditure					**(6,180)**	**(6,413)**	**(233)**

Financial Statements: proposed opinion and audit differences

Balance Sheet as at 31 March 2015			
£'000	**Pre-audit**	**Post-audit**	**Audit Adjustment**
Total property, plant & equipment	**51,371**	**52,796**	**1,425**
Heritage Assets	334	334	0
Investment property	12,534	12,534	0
Long term investments	1,999	11,623	9,624
Long term debtors	320	320	0
Long term assets	**66,558**	**77,607**	**11,049**
Short term investments	12,300	2,676	(9,624)
Inventories	34	34	0
Short term debtors	6,771	6,513	(258)
Cash and cash equivalents	8,276	9,264	(988)
Current assets	**27,381**	**18,487**	**(8,894)**
Short term creditors	(9,568)	(11,376)	(1,808)
Current liabilities	**(9,568)**	**(11,376)**	**(1,808)**
Long term creditors	(136)	(136)	0
NDR Provision for Appeals	(1,280)	(1,280)	0
Other long term liabilities – Pensions	(38,310)	(38,310)	0
Long term liabilities	**(39,726)**	**(39,726)**	**0**
Net assets	**44,645**	**44,992**	**347**
General Fund balance	(3,761)	(2,703)	1,058
Capital receipts reserve	(903)	(809)	94
Government grants Unapplied	(14)	(14)	0
Earmarked reserves	(16,955)	(16,622)	333
Usable reserves	**(21,633)**	**(20,148)**	**1,485**
Revaluation reserve	(25,372)	(25,385)	(13)
Capital adjustment account	(37,300)	(38,712)	(1,412)
Deferred capital receipts	(23)	(23)	0
Available for sale financial instrument reserve	(144)	(144)	0
Pensions reserve	38,310	38,310	0
Collection fund adjustment account	1,382	975	(407)
Accumulated absences account	135	135	0
Unusable reserves	**(23,012)**	**(24,844)**	**(1,832)**
Total reserves	**(44,645)**	**(44,992)**	**(347)**

Financial Statements: proposed opinion and audit differences

Cash Flow Statement for Year Ending 31 March 2015		
£'000	**Pre-audit**	**Post-audit**
Net (surplus) or deficit on the provision of services	2,551	(2,717)
Adjust net surplus or deficit on the provision of services for noncash movements	686	(2,143)
Adjust for items included in the net surplus or deficit on the provision of services that are investing and financing activities	(751)	2,632
Net cash (inflows)/outflows from operating activities	**2,486**	**(2,228)**
Investing activities	(6,068)	9,792
Financing activities	(3,378)	(39)
Net (inflows)/outflows in cash and cash equivalents	**(6,960)**	**7,525**
Cash and cash equivalents at the beginning of the reporting period	15,236	16,789
Cash and cash equivalents at the end of the reporting period	**8,276**	**9.,264**
Movement in cash	**(6,960)**	**7,525**

Financial Statements: proposed opinion and audit differences

Movement in Reserves Statement for Year Ending 31 March 2015 (Pre-audit)

£'000	General Fund Balance	Earmarked GF Reserves	Capital Receipts Reserves	Capital Grants Unapplied	Total Usable Reserves	Unusable Reserves	Total Council Reserves
Opening balance	**(2,415)**	**(16,522)**	**(2,063)**	**(14)**	**(21,014)**	**(17,467)**	**(38,481)**
(Surplus) or deficit on provision of services	(1,886)	0	0	0	(1,886)	0	(1,886)
Other comprehensive income and expenditure	0	0	0	0	0	(3,539)	(3,539)
Total comprehensive income and expenditure	**(1,886)**	**0**	**0**	**0**	**(1,886)**	**(3,539)**	**(5,425)**
Adjustments between accounting basis & funding basis under regulations	772	0	1,160	0	1,932	(2,006)	(74)
Net (increase)/ decrease before transfers to earmarked reserves	**(1,114)**	**0**	**1,160**	**0**	**46**	**(5,545)**	**(5,499)**
Transfers (to)/ from earmarked reserves	(447)	447			0		0
(Increase)/ decrease in year	**(1,561)**	**447**	**1,160**	**0**	**46**	**(5,545)**	**(5,499)**
Closing balance	**(3,976)**	**(16,075)**	**(903)**	**(14)**	**(20,968)**	**(23,012)**	**(43,980)**

Movement in Reserves Statement for Year Ending 31 March 2015 (Post-audit)

£'000	General Fund Balance	Earmarked GF Reserves	Capital Receipts Reserves	Capital Grants Unapplied	Total Usable Reserves	Unusable Reserves	Total Council Reserves
Opening balance	**(2,415)**	**(16,522)**	**(2,063)**	**(14)**	**(21,014)**	**(17,740)**	**(38,754)**
(Surplus) or deficit on provision of services	(2,717)	0	0	0	(2,717)	0	(2.717)
Other comprehensive income and expenditure	0	0	0	0	0	(3,696)	(3,696)
Total comprehensive income and expenditure	**(2,717)**	**0**	**0**	**0**	**(2,717)**	**(3,696)**	**(6,413)**
Adjustments between accounting basis & funding basis under regulations	2,154	0	1,254	0	3,408	(3,408)	0
Net (increase)/ decrease before transfers to earmarked reserves	**(563)**	**0**	**1,254**	**0**	**691**	**(7,104)**	**(6,413)**
Transfers (to)/ from earmarked reserves	100	(100)	0	0	0	0	0
(Increase)/ decrease in year	**(463)**	**(100)**	**1,254**	**0**	**691**	**(7,104)**	**(6,413)**
Other CIES	**176**	**0**	**0**	**0**	**176**	**0**	**176**
Closing balance	**(2,702)**	**(16,622)**	**(809)**	**(14)**	**(20,147)**	**(24,844)**	**(44,991)**

Financial Statements: significant risks and key areas of audit focus

We have worked with the Authority throughout the year to discuss significant risks and key areas of audit focus.

This section sets out our detailed findings on the significant risk identified.

In our External Audit Plan 2014/15 we identified significant risks affecting the Authority's 2014/15 financial statements. The table below sets out our detailed findings in respect of these significant audit risks.

Significant audit risk: changing the general ledger	
Issue	**Findings**
A new Civica general ledger system went live on 1 April 2014, during which existing balances were transferred from the old Oracle system to Civica. There is a risk therefore that information was not migrated over accurately or completely, which could result in the misstatement of opening balances.	We undertook the following procedures in response to this risk: • We reviewed the assurance report which the Authority's external consultant produced over the transition of balances onto the new ledger. This report only reviewed net total balances from Oracle to Civica, not the full balance sheet on a line by line level. • We reconciled the opening balances recorded on Civica on 1 April 2014 to the 2013/14 audited financial statements to ascertain if balances had been brought over correctly onto the new ledger. We identified that cash and investments balances totalling £12.4m had been misclassified when they were brought over to the new ledger. This was because Civica had more general ledger codes than previously, and hence now investments were split out between cash equivalent, short term investment, and long term investment in the general ledger. Previously these were all recorded together and then manually split out into their respective accounts lines as part of the year end accounts production process. This change led these transactions to be erroneously misclassified in the new ledger. These errors have been identified during the audit process and adjusted by the Authority. The full details of these are given in Appendix 3. We have raised a recommendation regarding the robustness of the assurance process undertaken over the new ledger implementation in Appendix 1.

Financial Statements: significant risks and key areas of audit focus

Significant audit risk: valuation of land, buildings and investment properties	
Issue	**Findings**
In 2013/14 the Authority reported that it owned land and buildings valued at £36.1m and Investment Properties of £10.3m. Local Authorities exercise judgment in determining the fair value of different asset classes held and the methods used to ensure that the carrying values recorded each year reflect those fair values. Given the materiality in value and the judgment involved in determining the carrying amounts of assets, we identified through our audit fieldwork that the valuation of land, buildings and investment properties should be a significant audit risk for 2014/15. At 31 March 2015 the Authority reported in its draft financial statements that it owned land and buildings valued at £48.4m and Investment Properties of £12.5m.	In 2014/15, the Authority commissioned Wilks, Head and Eve (WHE) LLP to undertake a revaluation exercise on a selection of its land and buildings as at 1 April 2014, in line with its accounting policy to ensure that all assets are revalued over a five year period. The total revalued value of land and buildings in the draft financial statements was £25.8m, and investment properties was £12.5m, valued as at 1 April 2014. We considered the independence and experience of WHE. We were satisfied that the valuer was appropriately qualified to undertake the valuation, and that it was conducted in accordance with RICS principles and the Authority's accounting policies for Property, Plant and Equipment and Investment Properties, and the instructions provided. We have also undertaken a review to confirm that the valuation bases adopted for each class of assets are in line with appropriate industry bases. We have reviewed the revaluation instructions provided to the Authority's external valuers, Wilks Head and Eve, and the revaluation report received by the Authority confirming the properties revalued, the type of properties, the valuation bases and the property information used. We reviewed the accounting entries made by the Authority to confirm that the valuations provided by WHE were correctly recorded in the financial statements. Here we identified that the Authority had incorrectly charged the full value of an impairment of £1.6m for Camberley Theatre to the Comprehensive Income and Expenditure Statement (CIES). This asset had a corresponding balance in the revaluation reserve of £1.4m, therefore this impairment should have been charged against the revaluation reserve first, before the remaining £200k was charged to the CIES. This error has been amended by the Authority in the revised financial statements. We also considered the Authority's arrangements for assessing the potential for material changes in valuation of property between the valuation date (1 April 2014) and the Balance Sheet date (31 March 2015). In response to an audit request, the Authority commissioned an impairment and valuation review be undertaken by their external valuer. This confirmed that there had not been a material impairment to the Authority's asset portfolio between the valuation date and the balance sheet date. It also confirmed that there had been no significant increase in value in investment properties. WHE's analysis of the property market for land and buildings which had been revalued determined with reference to publicly available indices, that there had been a material increase in the value of these properties between the valuation date and the balance sheet date. In order to meet the *Code of Practice on Local Government Accounting in the UK 2014/15* requirement that the fair value of revalued assets are not materially different to their carrying value, the Authority therefore uplifted the value of these revalued assets by 7.9%, totalling £1.4m. We have raised a recommendation regarding this matter in Appendix 1.

Financial Statements: significant risks and key areas of audit focus

Significant audit risk: management override of controls	
Issue	**Findings**
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 due to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We have not identified any specific additional risks of management override relating to this audit. Our audit methodology incorporates the risk of management override as a default significant risk for 2014/15.	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.

Financial Statements: accounts production and audit process

The Authority's finance team experienced challenges in preparing the draft accounts in 2014/15, and this is reflected in the quality of draft accounts produced.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about 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. We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	The Authority's financial reporting processes faced challenges this year, in particular as a result of the new Civica ledger which was implemented on 1 April 2014. As a result, financial reporting processes were not as strong as would have been required in order to produce draft financial statements of an appropriate quality. We have identified a higher number of errors in the accounts than in previous years, and in some areas of the accounts, for example Note 11 Property, Plant and Equipment; Financial Instruments; Cash; the Movement in Reserves Statement; and the Cashflow Statement, changed substantially during the course of audit fieldwork. We consider that accounting practices are generally appropriate, however the larger than expected volume of errors has distorted the presentation of these in the draft financial statements.
Completeness of draft accounts	The deadline for draft accounts to be submitted for audit was 30 June 2015 as set by the DCLG. The Authority did not meet this deadline as we received the draft accounts on 8 July 2015. The Authority also missed the deadline for the first cycle submission of the WGA on the 10 July 2015 as set by the DCLG. This was submitted by the Authority on the 29 July 2015. The Authority was not able to provide to audit sufficient supporting evidence for some balances reported in the draft financial statements. This resulted in the Authority missing the DCLG audit accounts submission deadline of 30 September 2015, and the WGA audit submission deadline of 2 October 2015.
Quality of supporting working papers	The quality of working papers provided did not consistently meet the standards specified in our PBC request list. In several cases, including payroll, financial instruments, cash and debtors, supporting working papers did not reconcile to the financial statements.
Response to audit queries	Officers made significant efforts to address audit queries in a timely fashion. However, a more timely response was not possible due to staff sickness and annual leave during the audit. Moreover, the structure of the finance team; whereby it was rare for a single officer to have full responsibility for any specific accounts area, meant that there were delays due to input being required from multiple members of the finance team.
Prior year recommendations	As part of our audit we have specifically followed up the Authority's progress in addressing the recommendations in previous years' ISA 260 reports. The Authority has implemented two out of seven recommendations raised in our 2013/14 and 2012/13 ISA 260 Reports. Appendix 2 provides further details.

Financial Statements: completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's 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 Surrey Heath Borough Council for the year ending 31 March 2015, we confirm that there were no relationships between KPMG LLP and Surrey Heath Borough Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 4 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 the Head of Finance for presentation to the Audit and Standards 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 parties, 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.

VFM conclusion

Our VFM conclusion considers how the Authority secures financial resilience and challenges how it secures economy, efficiency and effectiveness.

We have concluded that overall the Authority has not made proper arrangements to ensure financial resilience and to secure economy, efficiency and effectiveness in its use of resources due to a lack of staff capacity in the finance team and in the management of major capital projects.

Background

Auditors are required to give their statutory VFM conclusion based on two criteria specified by the Audit Commission. These consider whether the Authority has proper arrangements in place for:

- securing financial resilience: looking at the Authority's financial governance, financial planning and financial control processes; and
- challenging how it secures economy, efficiency and effectiveness: looking at how the Authority is prioritising resources and improving efficiency and productivity.

We follow a risk based approach to target audit effort on the areas of greatest audit risk. We consider the arrangements put in place by the Authority to mitigate these risks and plan our work accordingly.

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

Work completed

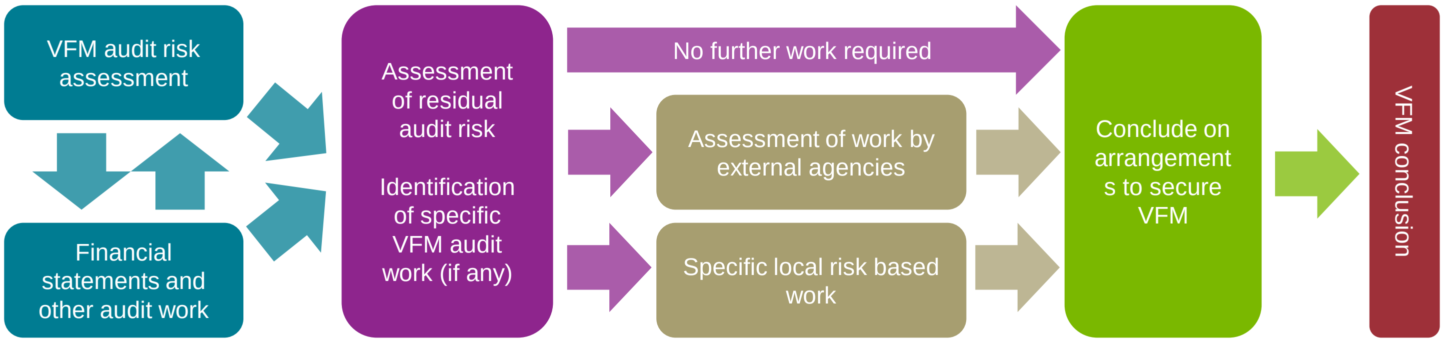
We performed a risk assessment earlier in the year and have reviewed this throughout the year.

We keep this risk assessment continually under review. During audit, we identified a significant risk to our VFM conclusion in relation to the capacity and capability within the finance function, leading to the inconsistent application of core elements of the financial control environment.

This was identified through interim fieldwork which identified that key financial controls had not taken place throughout 2014/15. Moreover, receipt of the draft financial statements in July 2015 identified significant a large volume of audit adjustments, and the financial statements and WGA were submitted late. The Authority was unable to provide sufficient supporting evidence for some balances reported in the draft financial statements, and as a result the Authority missed the DCLG accounts submission deadline of 30 September 2015, and the WGA submission deadline of 2 October 2015. Therefore in line with the audit approach as directed by the Audit Commission, we identified staff capacity within the finance team and the application of core elements of the financial control as significant risks to the VFM conclusion, and undertook additional work in this area as appropriate.

Conclusion

We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources and to ensure financial resilience in 2014/15, except for capacity in the finance team and the application of core elements of the financial control environment. These have resulted in the inconsistent application of key financial controls during the year, and in the production of financial statements which did not meet statutory deadlines or audit quality standards.



Specific VFM risks

We identified a specific VFM risk during the course of our audit in relation to capacity in the finance team and in regard to the application of core financial controls.

We undertook additional testing procedures in response. From the outcome of this testing we were unable to conclude that the internal controls provide sufficient assurance that the Authority's current arrangements in relation to this risk area is adequate.

Work completed

In line with the risk-based approach set out on the previous page and in response towards a risk concerning budget monitoring identified during the audit process, we have:

- assessed the Authority's key business risks which are relevant to our VFM conclusion;
- identified the residual audit risks for our VFM conclusion, taking account of work undertaken in previous years or as part of our financial statements audit;
- considered the results of relevant work by the Authority, inspectorates and review agencies in relation to these risk areas; and
- completed specific local risk based work on the Authority's budget monitoring procedures.

Key findings

Below we set out the findings in respect of those areas where we have identified a residual audit risk for our VFM conclusion.

We concluded that we needed to carry out additional work for the identified specific risk. This work is now complete and we also report on this below.

Key VFM risk: capacity of the finance team and inconsistent application of core financial controls	
Issue	**Findings**
On 1 April 2014 the Authority implemented a new Civica general ledger. Discussions with officers has identified that this project was not planned or resourced sufficiently to ensure project success and when issues arose, they were not resolved in a timely fashion to ensure the impact was minimised. This, in addition to structural and capacity issues within the finance team, has meant that "business as usual" could not continue throughout the implementation phase, and implementation difficulties impacted on the application of core financial controls throughout 2014/15.	We reviewed the project plan for the Civica implementation and held discussions with senior officers. We also undertook detailed testing of core financial controls during year, specifically bank reconciliations and budget monitoring. We identified that the Authority was not able to correctly reconcile the General Ledger to the bank during 2014/15. The first month where the bank reconciliation was undertaken correctly was for March 2015, undertaken in June 2015. Moreover, the Authority was unable to correctly profile its budgeted expenditure across the year. As a result, budget monitoring could not be undertaken on a budget vs actuals basis, but rather departments were asked to predict if their year end balance would vary from budget by £10k or more. Implementation difficulties meant that these key financial controls could not be appropriately undertaken in year, and that "business as usual" could not continue throughout the implementation phase. We also reviewed the Authority's closedown plan for producing the annual accounts. It was similar to previous years' plans, however did not take account of the ledger implementation difficulties or the staff resources which were required to address these, rather than prepare the annual accounts. The plan also did not take account of staff leave during the accounts production process. *(Continued overleaf)*

Specific VFM risks (continued)

Key VFM risk: capacity of the finance team and inconsistent application of core financial controls (continued)

Findings

The draft financial statements and WGA DCT pack were submitted late, missing the DCLG deadlines. The draft financial statements contained a large volume of errors, and the primary statements did not reconcile to one another. Discussions with officers has identified capacity and structural difficulties within the finance team which put at risk their ability to deliver their statutory responsibilities.

This underlines that the finance team lacked an appropriate level of quality control review of the draft financial statements, and that there was not an appropriate plan in place to ensure the finance team structure and resources could be utilised effectively to meet statutory responsibilities. The structure of the finance team is also currently under review.

As a result of this, we were not able to gain the assurance sought to mitigate the risk identified over the lack of capacity within the finance team and the inconsistent application of core financial controls. Recommendations regarding these matters have been raised in Appendix 1.

In light of the above we have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources and to ensure financial resilience in 2014/15 except for in regard to capacity within the finance team and the application of core financial controls, which has impact on the Authority's financial control and efficiency and productivity in 2014/15.

As a result of the issues described above, our opinion on the Authority's Use of Resources conclusion will be:

In considering the Authority's arrangements for securing financial resilience and challenging how it secures economy, efficiency and effectiveness we identified the following matters:

- ***Inconsistent application of core elements of the financial control environment:*** *The Authority faced a number of challenges following the introduction of a new financial ledger system on 1 April 2014. It had a detrimental impact on the consistency with which fundamental financial controls were applied in year. For example, no bank reconciliations were performed during 2014/15 and there were significant delays in the preparation of the year-end bank reconciliation as at 31 March 2015. The ledger implementation also meant that the regular monitoring of actual expenditure against budgets did not take place during 2014/15.*
- ***Capacity, capability and structure of the finance function:*** *The submission deadlines for the unaudited draft accounts and the Whole of Government Accounts (WGA) pack were not met by the Authority. Once received, the draft accounts required a significant number of material adjustments to be made which corrected the outturn position of the Authority. These capacity and capability issues are compounded by pressures within the resource model of the finance function, the structure of which is under review.*

Conclusion

On the basis of our work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2014, with the exception of the matters reported in the basis for qualified conclusion paragraph above, we are satisfied that, in all significant respects, Surrey Heath Borough Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2015.

Appendix 1: Key issues and recommendations

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

The Authority should closely monitor progress in addressing specific risks and implementing our recommendations. We will formally follow up these recommendations next year.

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 don't need immediate action. You may still meet a system objective in full or in part or 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.

No	Risk	Issue and recommendation	Management response / responsible officer / due date
1	❶	**Accounts production quality assurance framework** In the draft financial statements submitted for audit, 44 significant errors were identified, of which 21 were material. Of the 44 errors, 25 impacted the prime financial statements. A key contributor to this was the reduced level and robustness of quality assurance over the draft financial statements in 2014/15 than in previous years. Moreover, the Authority submitted its draft financial statements for audit on 8 July, missing the submission deadline of 30 June. The Authority submitted its draft Whole of Government Accounts ("WGA") pack on 29 July, missing the Department of Communities and Local Government ("DCLG") deadline of 10 July. The Authority was unable to provide sufficient supporting evidence for some balances reported in the draft financial statements, and as a result the Authority missed the DCLG accounts submission deadline of 30 September 2015, and the WGA submission deadline of 2 October 2015. **Recommendation** The Authority should develop a more robust quality assurance framework for the production of its financial statements. This should include a built in timetable for the production of the accounts, which is adhered to, with key individuals allocated responsibility for specific items to ensure accountability. This should be designed to ensure that there is contingency and cover available in the event that team members are unavailable for any reason. This should also include layers of appropriate quality review to ensure the draft accounts are of appropriate quality before they are submitted for error. This should help to ensure that the volume of errors and presentational amendments identified are resolved and do not reoccur.	**Agreed** As in previous years an accounts preparation timetable was prepared for 2014/15. This allocated individual tasks to staff for areas of the financial statements and there were regular meetings held to monitor progress. However due to operational issues the timetable slipped and the deadline was missed. We will ensure that for next year the timetable is adhered to fully to ensure that the accounts are produced on time. This will include sufficient time to enable a quality review to be done to highlight any potential errors before publication. Where possible contingency cover will be identified however this may not be possible for all areas given the size of the finance department. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** 30 June 2016

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
2	❶	**Budget monitoring** Our review of the Authority's budget monitoring arrangements identified that the Authority was not able to profile its budgeted expenditure correctly using the new Civica ledger system in 2014/15. As a result, the Authority was not able to undertake budget monitoring of budget vs actuals in year. Instead, the Authority undertook monitoring of actuals vs year end forecast outturn at a service level. This type of budget monitoring had been undertaken in prior years, and KPMG had previously raised a recommendation that this monitoring should be undertaken on a real time actuals basis. **Recommendation** We recommend that the Authority undertakes budget monitoring comparing actual income and expenditure against budgeted income and expenditure. This analysis should be regularly reported to the Executive so they have an accurate and up to date understanding of the Authority's financial position.	**Agreed** In 2014/15 all the budgets were profiled in 12ths as part of the setup for the new computer system. This meant that monitoring actuals to budget could not be relied upon to give an accurate picture. For 2015/16 Budget Monitoring is being performed by comparing budget to date v actuals as in the recommendation. Service Heads have been tasked with ensuring that budgets for the year have been profiled correctly so as to ensure that the monitoring reports are accurate. Executive Members receive copies of all the monitoring reports produced by Civica each month showing service variances with significant variances, which may have an impact on outturn, being reported formally to Executive every quarter. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** Implemented

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
3	❶	**Cut-off testing** From our initial cut-off sample testing, we identified one receipt of £188k in March 2015 incorrectly coded to April in the 2015/16 financial year. Also we identified a further two cut-off related errors, amounting to a gross value of £72k from our CIES non-pay expenditure testing whereby these transactions had been posted to the incorrect financial year. **Recommendation** Our analysis does not indicate that this could lead to a material misstatement, however we recommend that the Authority reinforces its process for accruing income and expenditure transactions appropriately at year end and ensures there is a robust process in place for posting relevant transactions to the correct financial year.	**Agreed** The Council operates a very short window to process prior year transactions before the month is closed. This means that invoices arriving late have to be accrued. Next year we will put in processes to ensure that income and expenditure is recognised in the correct period. The transactions team has reviewed the procedures to check periods covered on supplier invoices were quoted to ensure that accruals and prepayments are picked up and adjusted for. In addition procedures have been updated to check that invoices received after year end to ensure that expenditure is accounted for in the correct period. **Responsible Officer** Sarah Parmenter, Senior Accountant **Due Date** 30 June 2016

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
4	1	**Bank reconciliations** Due to issues around the configuration and interfacing of the bank reconciliation module within Civica the first time the Authority could reconcile its bank to the General Ledger in 2014/15 was for the month of February 2015. However, this bank reconciliation did not agree to underlying audit trails and did not appropriately reconcile the bank account balance to the general ledger. The Authority then undertook a year end exercise to prepare the year end bank reconciliation in June 2015, and this has been found to appropriately reconcile the bank to the ledger. However, this key control did not operate effectively throughout 2014/15. **Recommendation** Regular reconciliations of the bank account to the general ledger are an essential internal control which enables any discrepancies with regards to cash to be identified and resolved in a timely manner. We therefore recommend that management perform bank reconciliations on a monthly basis, to ensure that any discrepancies are identified and resolved in a timely manner. These bank reconciliations should be separately prepared and authorized to ensure sufficient segregation of duties.	**Agreed** Discussions began with Civica in May 2014 when it was discovered that the bank reconciliation module did not function as expected. This was due to issues around the interfaces with various other computer systems. Despite protracted discussions with Civica it took until April 2015 for the issue to be resolved sufficiently for a bank reconciliation to be done. In 2015/16 the bank has been satisfactorily reconciled every month up to the 31 August and no errors identified. **Responsible Officer** Sheena Adrian, Capital Accountant **Due Date** Implemented

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
5	❶	**Assurance over opening balances** On 1 April 2014, the Authority transitioned to a new Civica ledger system, from the former Oracle ledger system. In June 2015, the Authority commissioned a piece of assurance work by an external consultant over the integrity and accuracy of balances transferred from the old to the new ledger. This reviewed all balance sheet items, though only at a net balance level, balances were not mapped on a line by line basis. We undertook detailed testing of the balances transferred to the new ledger, by mapping balances on Civica on 1 April 2014 back to the 2013/14 audited financial statements. We identified that there were misclassifications between debtors and creditors, and cash and investments balances, on the opening ledger on 1 April 2014. These were due to mapping differences between Oracle and Civica; previously these items would have required a year end off ledger adjustment to classify them appropriately in the financial statements. Civica provides the functionality to record these appropriately. Discussions with officers confirms that these reclassifications were identified by the assurance work undertaken however these were not amended on the ledger. This resulted in errors in the 2014/15 draft financial statements. **Recommendation** We recommend that when there is a data migration exercise in any system, the data is initially migrated on a like-for-like basis and assurance work performed over the data transferred, before any subsequent reclassifications are undertaken. This will reduce the likelihood of misclassifications arising during the data migration exercise not being readily identifiable. Moreover, we recommend that any work performed by consultants or other experts are subject to review at a higher level of detail, to ensure that any arising discrepancies are identified and can be actioned in a timely fashion. This will help to ensure that the Authority utilizes their expertise appropriately and ensures value for money for the services paid for.	**Agreed** We note your recommendation and will ensure that balances are transferred on an individual basis were we to transfer to a new financial system in the future. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** Immediate

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
6	1	**Movement in Reserves Statement and Cashflow Statement** The revised financial statements produced by the Authority include a MiRS and a Cashflow Statement which contain variances between these statements and the balance sheet and CIES. We are satisfied that these balances are not material, however these do represent significant differences between the primary statements. We have raised these as unadjusted differences in Appendix 3 of this report. **Recommendation** We recommend that when preparing the 2015/16 financial statements, the Authority ensures it prepares all the primary statements in line with the *Code of Practice on Local Authority Accounting 2015/16*, to ensure that all statements reconcile correctly. Appropriate time should be set aside as part of the closedown process to ensure that all the statements can be prepared correctly, and all staff involved in the process are sufficiently familiar with the technical accounting requirements of the *Code of Practice on Local Authority Accounting 2015/16*, to ensure a high quality set of financial statements.	**Agreed** Staff have undertaken training on the changes to the Code of Practice on Local Authority Accounting and we have employed additional resources to assist with the preparation of accounts and to ensure that they meet the required standard. We will work closely with the auditors at an early stage on complex technical accounting issues so as to ensure that our interpretation aligns with theirs thereby reducing differences. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** 30 June 2016
7	2	**Documenting budget monitoring** The Authority's budget monitoring process during 2014/15 involved asking service areas to compare actuals vs year end forecast outturn on a quarterly basis. However, some budget monitoring discussions undertaken between finance staff and officers in service areas is not documented. Rather, it is done through conversation only. This raises the risk that crucial budgeting information or explanations are not retained, with no record or audit trail to refer back to at a later date. **Recommendation** We recommend that all budget monitoring discussions are formally documented. A standard template could be developed for this to ensure that all pertinent details are always recorded in meetings, to ensure that information is retained in a complete and consistent manner.	**Agreed** Budget monitoring arrangements and discussions will be documented going forward. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** 30 April 2016

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
8	2	**Revaluations of property, plant and equipment, and investment properties** The Authority revalued land and buildings in line with their five year rolling revaluation programme, and all investment properties as at 1 April 2014, as part of the rolling programme of revaluations. The *Code of Practice on Local Authority Accounting in the United Kingdom 2014/15 ('the Code')* requires that Authorities satisfy themselves that where there has been a revaluation, that the difference between the carrying value of the assets on the balance sheet, and their fair value, is not materially different. The Authority did not undertake an exercise to satisfy itself that there was not a material difference in the value of assets between the valuation date of 1 April 2014, and the balance sheet date of 31 March 2015. When requested by KPMG, the Authority's external valuers, Wilks Head and Eve, carried out a year end market review, and then subsequently undertook analysis against market indices to ascertain if the value of revalued assets had materially increased during the year. This led to an audit adjustment of £1.078m for land and buildings; there was not change in the valuation of investment properties. **Recommendation** We recommend that each year, as part of the accounts production process, the Authority should undertake both an impairment review, and analysis to ascertain the impact of any market increase, between the valuation date and the balance sheet date. This will ensure that revalued assets are valued at a materially appropriate value within the financial statements.	**Agreed** The Council will commission and impairment and market revaluation review from its valuers as part of the annual property valuation process **Responsible Officer** Sheena Adrian, Capital Accountant **Due Date** 30 June 2016

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
9	2	**Debriefing major projects to identify lessons learnt** The Authority implemented the new Civica ledger system on 1 April 2014. Full functionality was not implemented within the original timescales and this has resulted in a delay in implementing a 'business as usual' state. This increased pressure on the finance team's already challenging resource model and impacted on the quality of outputs, as the finance team had to concurrently manage both ledger implementation difficulties and day to day tasks. **Recommendation** We recommend that the finance team undertake a debrief workshop to learn lessons from the Civica implementation, to ensure that opportunities to improve future project implementations are identified and taken forward appropriately. This should be undertaken within an appropriate timeframe, with sufficient time to have lapsed between the end of the project and the debrief, to allow for staff reflection and consideration before the workshop. Such debrief workshops should be held after all significant project implementations to ensure that all such opportunities for learning are identified to enhance the Authority's project management and delivery arrangements.	**Agreed** The finance team will undertake this debrief for the Civica implementation project, and further debriefs will be undertaken at the end of major projects. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** 30 April 2016

Appendix 1: Key issues and recommendations

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
10	3	**Journal authorization** The Authority has a two stage journals authorisation process in place; all journals are required to be authorised by an officer separate to the preparer. All journals over £20k are also required to be second authorised by the Head of Finance. Our detailed testing found that out of 18 journals over £20k tested, 7 had not been second authorised. We note that the journals we tested appeared reasonable and each had adequate supporting evidence. We are also satisfied that effective segregation of duties is in place, as the journals had been authorised by an officer separate to the preparer in all cases. However, the failure to adhere to this policy increases the risk that erroneous or incorrect amendments might be made in the ledger without detection. **Recommendation** We recommend the Council review its procedures for the authorisation of journals. If it is determined that the current process is appropriate for the Authority's operations, then this should be appropriately communicated to all relevant staff to ensure this policy is complied with going forward.	**Agreed** The policy will be reviewed to ensure that only major journals, over £100k, need to be countersigned by the Executive Head of Finance. **Responsible Officer** Kelvin Menon, Executive Head of Finance **Due Date** 30 April 2016

Appendix 2: Follow up of prior year recommendations

The Authority has not implemented all of the recommendations in our *ISA 260 Report 2013/14 and 2012/13.*

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 *ISA 260 Report 2013/14 and 2012/13* and re-iterates any recommendations still outstanding.

Number of recommendations that were:	2013/14	2012/13
Included in original reports:	1	6
Implemented or superseded:	0	3
Remain outstanding or reoccurring in 2014/15 (re-iterated below):	1	3

No.	Risk	Issue and recommendation	Status as at March 2016
1	3	**Cut off testing (2013/14)** For four items in our cut-off testing sample, all relating to car parking income, we identified that cash had been collected on the last day of the financial year, but had not been banked and posted to the ledger until the first day of the new financial year. The total value was slightly above the threshold that the Authority considers for making accruals at the year end. Our analysis does not indicate that this could lead to a material misstatement, however, we recommend that the process for accruing for income and expenditure that is greater than the threshold value that the Authority has set is re-enforced and applied for future accounting periods.	**Reoccurring in 2014/15** Our 2014/15 audit has identified three errors in cut off. These errors are from different areas of the accounts and range in value from £11k to £188k. However, all are above the Authority's threshold for accruing income and expenditure.

Appendix 2: Follow up of prior year recommendations

The Authority has not implemented all of the recommendations in our *ISA 260 Report 2013/14 and 2012/13.*

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

No.	Risk	Issue and recommendation	Status as at March 2016
2	2	**Agreement of the financial statements to the ledger (2012/13)** The Authority did not prepare an adequate working paper to map the Balance Sheet and Comprehensive Income and Expenditure Statement to the ledger. As a result additional work was required during the audit by both the Council and the audit team to agree the financial statements to the ledger. The Authority should prepare and retain working papers that show how the financial statements have been derived from the ledger, providing an audit trail tracking the ledger balances, manual adjustments, and financial statements entries. This should be prepared as part of the closedown process prior to the audit commencing and should be subject to quality review.	**Reoccurring in 2014/15** In both 2013/14 and 2014/15, there was a delay in obtaining a working paper that adequately mapped the Balance Sheet and Comprehensive Income and Expenditure Statement to the ledger. This resulted in additional work during the audit by both the Council and the audit team to agree the financial statements to the ledger.
3	2	**Journal authorisation (2012/13)** Our audit work had identified that not all journals are authorised in line with the Authority's authorisation procedures, and there was a lack of documentation retained to support and explain the rationale for some journals. Without strong disciplines concerning the raising and authorisation of journals, there is an increased risk of errors in the financial statements. The journal process should be strengthened by: • reviewing a journal listing report of all high value journals to ensure they have been appropriately authorised; and • retaining documentation for all journals to explain the purpose of the journal.	**Reoccurring in 2014/15** We undertook journals controls testing during 2014/15, and out of 18 journals over £20k tested, 7 had not been second authorised in line with the Authority's policy. This recommendation has been raised in 2014/15, see Appendix 1.

Appendix 2: Follow up of prior year recommendations

The Authority has not implemented all of the recommendations in our *ISA 260 Report 2013/14 and 2012/13.*

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

No.	Risk	Issue and recommendation	Status as at March 2016
4	2	**Budgetary control (2012/13)** Our review of budgetary control noted that: • Finance reports to the Executive compare the forecast year end position against the budget. There is no detail of actual spend to date which would allow better to challenge the forecast; and • Budget variance explanations from service heads are not always received in a timely manner, meaning explanations are sometimes rolled forward from the prior month without update. Without strong financial management disciplines there is an increased risk of unforeseen overspends, particularly as funding cuts take effect. We recommend that finance reports to the Executive should detail actual spend to date as well as the forecast outturn. The Authority should also require all service heads to provide updated budget variance commentary on a monthly basis.	**Reoccurring in 2014/15** In 2013/14 this was reported as having been superseded in light of the new Civica ledger. It was considered that this would improve the quality of internal budget monitoring and reporting. However, as is detailed in Appendix 1, the Authority was not able to profile its budgeted expenditure correctly using Civica in 2014/15. As a result, the Authority was not able to undertake budget monitoring of budget VS actuals in 2014/15. We understand from Management that in Q1 of 2015/16, this profiling of expenditure has been resolved, such that real time monitoring reports are able to be produced. However, this was not possible during 2014/15.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

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

Uncorrected audit differences

Our audit has identified the following unadjusted errors:

	Impact
No.	**Disclosure**
1	The Cashflow Statement contains an audit difference of £83k. This is because the non cash adjustments line within the Cashflow Statement contains the value of revaluations to Other Land and Buildings. The value of this as the financial statements is £196k, however the value inserted into the Cashflow Statement for this item is £279k. This represents an unadjusted audit difference of £83k, which is immaterial to the financial statements.
2	The Movement in Reserves Statement contains a reconciling variance of £176k between the figures stated in the MiRS and the other primary statements and notes to the financial statements. This represents an unadjusted audit difference of £176k, which is immaterial to the financial statements.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

Corrected audit differences

The following table sets out the significant audit differences identified by our audit of Surrey Heath Borough Council's financial statements for the year ended 31 March 2015.

	Impact				
No.	**Income and Expenditure Statement**	**Assets**	**Liabilities**	**Reserves**	**Description of audit difference**
1	Dr Income £47k	Cr Short Term Debtors £47k			An invoice for £47k was incorrectly raised during 2014/15 in respect of work that had not yet been performed. The debtor was issued with a credit note for this work in July 2015 for the full amount. KPMG have confirmed that this was an isolated error.
2	Cr Depreciation, Amortisation & Impairment £1,412k			Dr Revaluation Reserve £1,412k	The land element of one asset (Camberley Theatre) was impaired by £1,612k. This asset had a carried forward value in the Revaluation Reserve of £1,412k, however, the full impairment was charged directly to the CIES. This impairment should, however, have initially reduced the Revaluation Reserve to nil, with the remaining £200k subsequently being charged to the CIES.
3	Dr Non Domestic Rates Income £857k	Cr Short Term Debtors £857k			The NNDR Safety Net accrual was overstated in short term debtors within the draft financial statements, representing an error of £857k.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

	Impact				
No.	**Income and Expenditure Statement**	**Assets**	**Liabilities**	**Reserves**	**Description of audit difference**
4	Dr Central Services Expenditure £420k Cr Central Services Income £246k Cr Income and Expenditure in relation to Investment Properties £174k				A ledger code was erroneously excluded from the Central Services accounts line. This resulted in an understatement of both income and expenditure, with the Central Services line within Net Cost of Services. The net balance of £174k impacts Income and Expenditure in relation to Investment Properties within the CIES.
5	Cr Cultural Services Expenditure £876k Dr Cultural Services Income £876k				A ledger code was erroneously double counted in both income and expenditure within Cultural Services in the CIES. Therefore both income and expenditure are overstated by this amount of £876k.
6	Dr Cultural, Environmental and Planning Services Income £1,190k Cr Cultural, Environmental and Planning Services Expenditure £923k		Cr Short Term Creditors £267k		Within the CIES, we identified £1,190k of Suitable Alternative Natural Green Space (SANGS) income that should not have been recognised by the Council and should therefore be removed from the accounts. The corresponding Expenditure and Creditors entries also require reversing to remove these from the CIES and Balance Sheet.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

	Impact				
No.	**Income and Expenditure Statement**	**Assets**	**Liabilities**	**Reserves**	**Description of audit difference**
7		Dr Plant, Property and Equipment £1,438k		Cr Surplus/Deficit on Revaluation of Non Current Assets £1,438k	A year end impairment and revaluation exercise undertaken by property valuers Wilks Head and Eve identified a revaluation increase in non-current assets of £1,438k. This represents the increase in the valuation of revalued properties between the carrying value as at 1 April 2014 (the revaluation date) and the fair value at the balance sheet date.
8		Dr Long Term Investments £9,624k Cr Short Term Investments £9,624k			£9,624k of investments were erroneously recorded as short-term investments, however testing identified that these assets were long-term investments.
9		Dr AUC Disposals £94k Cr AUC Additions £161k Dr Other Land and Buildings Additions £59k Dr Vehicles, Plant and Equipment Additions £8k			In Note 11, the Assets Under Construction (AUC) balance brought forward from prior year were re-allocated to other asset categories. However, these transfers were incorrectly netted off against additions (£963k), showing additions incorrectly at £802k. Transfers out of the AUC category to other PPE categories should be presented in a separate line within the Note. As £94k of AUC was written off during the year, this should be treated as a disposal for nil proceeds. The remainder of the balance (£67k) should be included in a separate line to the effect of 'Reclassifications within PPE' split between Other land and buildings and Vehicles, plant and equipment, and shown as a positive balance in the categories that assets have been transferred to.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

	Impact				
No.	**Income and Expenditure Statement**	**Assets**	**Liabilities**	**Reserves**	**Description of audit difference**
10		Dr Short Term Debtors Central Government £352k Dr Short Term Debtors Other Local Authorities £352k Cr Cash and Cash Equivalents £704k			A debtors balance of £704k relating to NNDR had been erroneously recoded to cash and cash equivalents, resulting in an overstatement of cash and an understatement of debtors.
11		Dr Short Term Debtors Central Government £123k Dr Short Term Debtors Other Local Authorities £123k Cr Cash and Cash Equivalents £246k			A debtors balance of £246k relating to Council Tax had been erroneously recoded to cash and cash equivalents, resulting in an overstatement of cash and an understatement of debtors.
12	Cr Non-Domestic Rates Income £76k	Dr Cash and Cash Equivalents £189k	Cr Short Term Creditors Central Government £94k Cr Short Term Creditors Other Local Authorities £19k		£189k of business rates income for 2014/15 had been accounted for in 2015/16 and so had been incorrectly excluded from the draft accounts. The full value is held as cash, and therefore the income must be appropriately apportioned between SHBC, Surrey County Council and Central Government.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

	Impact				
No.	**Income and Expenditure Statement**	**Assets**	**Liabilities**	**Reserves**	**Description of audit difference**
13	Dr Housing Services Income £283k Cr Adult Social Care Income £283k				Within the CIES, we identified that a £283k Disabled Facilities Grant included as income within Housing Services should have been coded to Adult Social Care.
14			Cr Short Term Creditors £333k	Dr Earmarked Reserves £333k	Per the draft financial statements, £333k held in the SANGS reserves requires reclassification as a short-term creditor as it relates to a credit balance owed to Hampshire County Council at the 2014/15 year end.
15	Cr Non Domestic Rates £129k		Dr Short Term Creditors Other Local Authorities £13k Dr Short Term Creditors Central Government £64k	Dr Collection Fund Adjustment Account £52k	Non-domestic rates income was understated by £129k in the draft CIES due to a miscoding of 2013/14 Transitional Protection income (176k) and Safety Net income (-£47k). This income must be apportioned to SHBC, Surrey County Council and Central Government in accordance with the appropriate percentages, and therefore adjustments to Income, Creditors, and the Collection Fund Adjustment Account are required.
16	Dr Non Domestic Rates £186k			Cr Collection Fund Adjustment Account £186k	Reversal of £186k adjustment that was made between v2 of the draft accounts and the final revised account. This related to SHBC share of the Collection Fund deficit for 2014/15.

Appendix 3: Audit differences

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

	Impact				
No.	Income and Expenditure Statement	Assets	Liabilities	Reserves	Description of audit difference
17		Dr Cash and Cash Equivalents £134k	Cr Short Term Creditors £134k		In the 2013/14 financial statements, £134k of cash held on behalf of a Trust in relation to Frimley Gravel and Sand had been omitted, and should have been included as both cash and a short-term creditor.
18		Dr Cash and Cash Equivalents £62k	Cr Short Term Creditors £62k		In the 2013/14 financial statements, £62k of cash held on behalf of the BIDS Collectively Camberley scheme had been omitted, and should have been included as both cash and a short-term creditor.
19		Dr Cash and Cash Equivalents £1,553k Cr Short Term Debtors £300k	Cr Short Term Creditors £976k	Cr Collection Fund Adjustment Account £277k	As at year end 2013/14, there was a negative cash contra item in respect of NDR within the cash balance that required reversing (£2,379k). Additionally, an amount relating to Council Tax owed to SHBC (£855k) that was netted off against this contra item also required reversing.

Appendix 3: Audit differences (Disclosure Amendments)

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

No.	Impact Disclosure	Basis of audit difference
20	The NNDR income figure changed from £33,666k to £34,131k between versions 1 and 2 of the accounts, reflecting a material difference of £465k.	The NDR income figure has changed materially between versions 1 and 2 of the accounts as a result of updated reconciliations undertaken during audit fieldwork.
21	In the draft accounts, Note 5 Assumptions and Estimates Made About the Future stated the sundry debtors balance at £2,400k. However, Note 20 Short Term Debtors stated that sundry debtors were £1,069k. This is a difference of £1,331k.	Within the final accounts, Note 5 should be updated to reflect the final values per Note 20 Sundry Debtors.
22	In Note 29, Related Parties, an error was identified in the 'Transactions with Members' section. The accounts stated that there was a total of £22k of transactions with Members, but on review of the supporting breakdowns this figure was shown to be £85k.	Transactions with members should be increased from £22k to £85k.
23	In Note 28, External Audit Costs, an error was identified within the 'fees payable for the certification of grant claims' line. This figure for 2014/15 should be £15k instead of the £11k reported in the draft financial statements. Consequently, the total for this Note should be £71k.	Fees payable for the certification of grant claims within Note 28 should be increased from £11k to £15k, and the total accordingly adjusted to £71k.
24	Within Note 30 Prior Period Adjustments, the narrative included a description of a change to the depreciation policy for officers' cars. This is not a material change and therefore does not meet the criteria for a Prior Period Adjustment under IAS 8.	The note regarding the change to depreciation policy should be removed from Note 30.
25	The wording per Note 17.5 of the draft accounts is incorrect as it does not make reference to non-domestic rates income.	Note 17.5 is to be revised so as to include non-domestic rates income per the Code of Practice on Local Authority Accounting.
26	Note 17.5 requires amending following revision of the Collection Fund accounts with respect to the Collection Fund Adjustment Account share of the revised deficit.	Note 17.5 is to be updated to reflect the Collection Fund Adjustment Account share of the revised Collection Fund deficit, after the required audit changes have been made.

Appendix 3: Audit differences (Disclosure Amendments)

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

No.	Impact Disclosure	Basis of audit difference
27	Within the draft financial statements, the value of leases held by the Council were incorrectly stated. This is because the draft note contained the equivalent value of 1 year's lease payment per lease, in the year in which the lease would expire. However, the Local Government Code requires that the future minimum value of lease payments, apportioned between the time periods in which the payments will be made, are presented. The following disclosures should therefore be made within Note 18.2: *2013/14* Not Later than 1 year: £172k 2-5 Years: £636k 5+ Years: £2,031k *2014/15* Not Later than 1 year: £232k 2-5 Years: £674k 5+ Years: £1,877k This Note also requires a narrative description regarding the Atrium and the nature of the contract, including the 2014/15 income (£240k) and the 2013/14 income (£174k), further stating that the contract is expected to continue for the foreseeable future.	Several disclosures need to included within Note 18.2 under both 2013/14 and 2014/15. A narrative description regarding the Atrium is also required.
28	The Surplus on provision of services per the Movement in Reserves Statement (MiRS) in the draft financial statements was £1,886k; in the CIES this figure was stated as £2,551k. This is a material difference of £665k.	Discrepancy between the Surplus on provision of services balance stated in the CIES to that stated in the MiRS.
29	In the CIES, Other Comprehensive Income and Expenditure was stated at £3,629k but listed as £3,539k within the MiRS, a difference of £90k. This variance was due to a transposition error in the CIES, where the surplus on the revaluation of PPE assets was entered as £9,328k as opposed to £9,238k.	Other Comprehensive Income and Expenditure per the CIES should be amended from £3,629k to £3,539k in order to remain in line with the values stated within the MiRS and Note 11 PPE.
30	In Note 34 Financial Instruments, it was identified that £8,123k of the Loans and Receivables balance within Long Term Investments of £11,623k related to Long Term Available for Sale Financial Assets.	Reduction of £8,123k from the Loans and Receivables balance within Long Term Investments.

Appendix 3: Audit differences (Disclosure Amendments)

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

No.	Impact Disclosure	Basis of audit difference
31	In Note 34, it was identified that the above £8,123k balance had been double counted and also included within 'Current Available for Sale Financial Assets.' This balance should be removed from this accounts line.	Reduction of £8,123k from the Current Available for Sale Financial Assets line within Note 34.
32	In Note 34, it was identified that a Current Loans and Receivables balance of £6,771k had been omitted from Note 34 in error. This balance should be included within this note.	Increase of £6,771k to Current Loans and Receivables in Note 34.
33	In Note 34, it was identified that a balance of £9,568k relating to 'Current Financial Liabilities Carried at Contract Amount' had been omitted from Note 34 in error. This balance should be included within this note.	Increase of £9,568k to Current Financial Liabilities Carried at Contract Amount in Note 34.
34	In Note 9 Adjustments Between Funding Basis and Accounting Basis, there is a £84k balance for Capital Expenditure Charged Against the General Fund. However this balance is £nil in Note 17.2 Capital Adjustment Account, hence is understated in Note 17.	Presentational amendment required to rectify an understatement of £84k in Note 17.
35	Several material adjustments have been made to Note 25 Amounts Reported for Service Allocation Decisions, as the figures stated did not reconcile to the CIES. Reclassifications and further subsequent audit adjustments within this note impact all lines.	Significant reclassification of Note 25 required in order for it to agree to the revised CIES.
36	Revenue expenditure amounting to £83k was incorrectly classified as a capital addition item before being impaired for during the year. Since the impairment has already been included as an expenditure item against the relevant service area, no change is required to the CIES. However, in Note 11 Property, Plant and Equipment, the additions figure for Other Land & Buildings needs to be reduced by £83k and the 'Revaluation Amount Recognised in the CIES' within this note needs to increase by £83k to reverse the amount impaired.	Decrease of £83k to Other Land and Building additions and increase of £83k to the 'Revaluation Amount Recognised in the CIES' within Note 11, Property Plant and Equipment.
37	The 'Revaluation Losses/Gains on PPE' balance within the Capital Adjustment Account in Note 17.2 was £1,691k. However, due to the £83k adjustment outlined above, and the £1,412k that should have been written back to the Revaluation Reserve, the actual CIES charge is £196k; this needs to be reflected within the Capital Adjustment Account.	Decrease of £1,495k to the Revaluation Losses/Gains on PPE from £1,691k to £196k within Note 17.2 Capital Adjustment Account.

Appendix 3: Audit differences (Disclosure Amendments)

This appendix sets out the significant audit differences identified during the audit for the year ended 31 March 2015.

We are reporting all adjusted audit differences over £45k.

It is our understanding that all of these will be adjusted.

No.	Impact Disclosure	Basis of audit difference
38	£1,691k was incorrectly classified as ‘Impairment Losses/Reversals Recognised in the Revaluation Reserve’ rather than in ‘Impairment Losses/Reversals Recognised in the Surplus/Deficit on the Provision of Services’ within Note 11, Property Plant and Equipment.	Reclassification of £1,691k from Impairment Losses/Reversals Recognised in the Revaluation Reserve to Impairment Losses/Reversals Recognised in the Surplus/Deficit on the Provision of Services within Note 11, Property Plant and Equipment.
39	Within Note 17.2, disposal for nil proceeds of £94k relating to Assets Under Construction have been omitted from the line ‘Amounts of Non Current Assets Written Off on Disposal or Sales as Part of the Gain/Loss on Disposal to the CIES.’	Note 17.2 must include the £94k relating to Assets Under Construction in the relevant line.
40	The Movement in Reserves Statement section within Note 31.2 Transactions relating to Post-Employment Benefits should be removed to remain in line with the Code.	Removal of the Movement in Reserves Statement section within Note 31.2 as it is not a required disclosure per the Code.
41	Due to the material audit adjustments listed above, the Cash Flow Statement and MiRS are subject to necessary material amendments. Similar adjustments are necessary for Note 9 Adjustments Between Accounting Basis and Funding Basis and Note 17 Unusable Reserves. The Explanatory Foreword and Annual Governance Statement will also require amendments where appropriate once the final accounts have been prepared.	Updates will be required to the Explanatory Foreword, Cash Flow and MiRS. Additionally, Notes 9, and 17 will require amendment to ensure consistency throughout the accounts following the audit adjustments detailed above.

Appendix 4: Declaration of independence and objectivity

The *Code of Audit Practice* requires us to exercise our professional judgement and act independently of both Public Sector Audit Appointments Ltd and the Authority.

Requirements

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

"Auditors and their staff should exercise their professional judgement and act independently of both the Commission and the audited body. Auditors, or any firm with which an auditor is associated, should not carry out work for an audited body that does not relate directly to the discharge of auditors' functions, if it would impair the auditors' independence or might give rise to a reasonable perception that their independence could be impaired."

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

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

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

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

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

General procedures to safeguard independence and objectivity

KPMG's reputation is built, in great part, upon the conduct of our professionals and their ability to deliver objective and independent advice and opinions. That integrity and objectivity underpins the work that KPMG performs and is important to the regulatory environments in which we operate. All partners and staff have an obligation to maintain the relevant level of required independence and to identify and evaluate circumstances and relationships that may impair that independence.

Appendix 4: Declaration of independence and objectivity

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

Acting as an auditor places specific obligations on the firm, partners and staff in order to demonstrate the firm's required independence. KPMG's policies and procedures regarding independence matters are detailed in the *Ethics and Independence Manual* ('the Manual'). The Manual sets out the overriding principles and summarises the policies and regulations which all partners and staff must adhere to in the area of professional conduct and in dealings with clients and others.

KPMG is committed to ensuring that all partners and staff are aware of these principles. To facilitate this, a hard copy of the Manual is provided to everyone annually. The Manual is divided into two parts. Part 1 sets out KPMG's ethics and independence policies which partners and staff must observe both in relation to their personal dealings and in relation to the professional services they provide. Part 2 of the Manual summarises the key risk management policies which partners and staff are required to follow when providing such services.

All partners and staff must understand the personal responsibilities they have towards complying with the policies outlined in the Manual and follow them at all times. To acknowledge understanding of and adherence to the policies set out in the Manual, all partners and staff are required to submit an annual ethics and independence confirmation. Failure to follow these policies can result in disciplinary action.

Auditor declaration

In relation to the audit of the financial statements of Surrey Heath Borough Council for the financial year ending 31 March 2015, we confirm that there were no relationships between KPMG LLP and Surrey Heath Borough Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

Appendix 5: Materiality and reporting of audit differences

For 2014/15 our materiality was £900k for the Authority's accounts.

We have reported all audit differences over £45k for the Authority's accounts to the Audit and Standards Committee.

Materiality

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 2014/15.

Materiality for the Authority's accounts was set at £900k which equates to c.2% of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision. During planning, this lower level of precision was set at £675k, equivalent to 75% of materiality. However, in response to the larger than anticipated volume of audit errors identified across the financial statements during audit fieldwork, it was determined that this level should be reduced. We therefore determined that a revised level of £450k would be appropriate, in order to detect significant errors to the Authority's financial statements.

Reporting to the Audit and Standards 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 and Standards 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 £45k 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 and Standards Committee to assist it in fulfilling its governance responsibilities.

Appendix 6: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

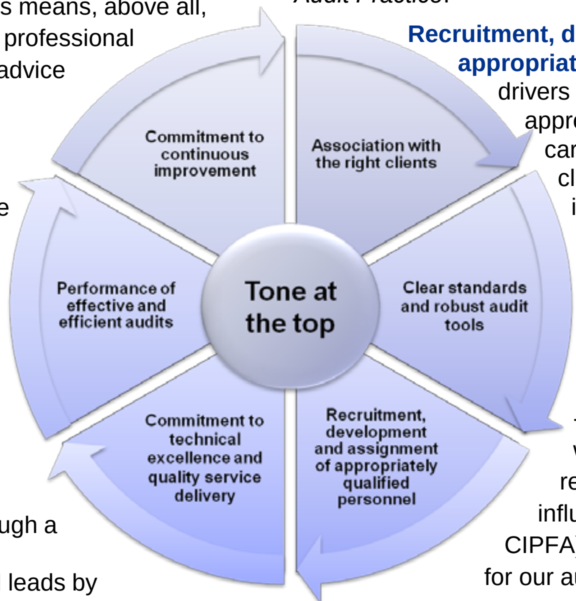
This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

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

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

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

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



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

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

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

Clear standards and robust audit tools: We expect our audit professionals to adhere to the clear standards we set and we provide a range of tools to support them in meeting these expectations. The global rollout of KPMG's eAudIT application has significantly enhanced existing audit functionality. eAudIT enables KPMG to deliver a highly technically enabled audit. All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.

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

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

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

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

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

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

Appendix 6: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

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

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

Commitment to technical excellence and quality service delivery: Our professionals bring you up- the-minute and accurate technical solutions and together with our specialists are capable of solving complex audit issues and delivering valued insights.

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

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

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

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

Our quality review results

Public Sector Audit Appointments Ltd publishes information on the quality of work provided by us (and all other firms) for audits undertaken on behalf of them (http://www.psaa.co.uk/audit-quality/principal-audits/kpmg-audit-quality/).

The latest Annual Regulatory Compliance and Quality Report issued June 2015 showed that we are meeting the overall audit quality and regulatory compliance requirements.

cutting through complexity™