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Report to those charged with governance (ISA 260) 2013/14

London Borough of Hammersmith and Fulham

16 September 2014

Contents

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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 has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.uk.

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

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Andrew Sayers the appointed engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 0303 4448 330.

Section one

Introduction

This document summarises:

- **the key issues identified during our audit of the financial statements for the year ended 31 March 2014 for both the Authority and its pension fund; and**
- **our assessment of the Authority's arrangements to secure value for money (VFM) in its use of resources.**

Scope of this report

This report summarises the key findings arising from:

- our audit work at London Borough of Hammersmith and Fulham ('the Authority') in relation to the Authority's 2013/14 financial statements and those of the Local Government Pension Scheme ('the Fund'); and
- our work to support our 2013/14 value for money (VFM) conclusion.

Financial statements

Our *External Audit Plan 2013/14*, presented to you in February 2014, set out the four stages of our financial statements audit process.

This report focuses on the second and third stages of the process: control evaluation and substantive procedures. Our on site work for these took place during February 2014 (interim audit) and July 2014 (year end audit).

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

VFM conclusion

Our *External Audit Plan 2013/14* explained our risk-based approach to VFM work, which follows guidance provided by the Audit Commission. We have now completed our work to support our 2013/14 VFM conclusion. This included:

- assessing the potential VFM risks and identifying the residual audit risks for our VFM conclusion;
- considering the results of any 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 2013/14 financial statements of the Authority and the Fund.
- 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.

Acknowledgements

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

Headlines

This table summarises the headline messages for the Authority and the Fund. Sections three and four of this report provide further details on each area.

Proposed audit opinion	We anticipate issuing an unqualified audit opinion on the Authority's financial statements by 30 September 2014. We will also report that the wording of your Annual Governance Statement accords with our understanding. We also anticipate issuing an unqualified audit opinion in relation to the Fund's financial statements, as contained both in the Authority's Statement of Accounts and the Pension Fund Annual Report by 30 September 2014.
Audit adjustments	Our audit has identified a total of two audit adjustments with a total value of £137.9m. The impact of these adjustments is to: ■ Increase the net worth of the Authority as at 31 March 2014 by £137.9 million, there is no impact on the general fund. We have included a full list of significant audit adjustments at Appendix 3. All of these were adjusted by the Authority. We have raised one recommendation in relation to the matters highlighted above in the relation to the valuation methodology and approach to PPE. This is set out in Appendix 1.
Key financial statements audit risks	We have worked with officers throughout the year to discuss specific risk areas. The Authority addressed all issues appropriately.
Accounts production and audit process	The Authority has good processes in place for the production of the accounts and high quality supporting working papers. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.
Control environment	The Authority's organisational control environment is effective overall, and we have not identified any significant weaknesses in controls over key financial systems.
Completion	At the date of this report our audit of the financial statements is substantially complete. Before we can issue our opinion we require a signed management representation letter, which covers the financial statements of both the Authority and the Fund. We will also need to complete our post balance sheet review procedures, covering the period up until the financial statements are signed. We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's and the Fund's financial statements.
VFM conclusion and risk areas	We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources. We therefore anticipate issuing an unqualified VFM conclusion by 30 September 2014.

Proposed opinion and audit differences

Our audit of the Authority's financial statements has identified a total of two audit adjustments.

The impact of these adjustments is to:

- **Increase the net worth of the Authority as at 31 March 2014 by £137.9 million.**

Proposed audit opinion

We anticipate issuing an unqualified audit opinion on the Authority's financial statements following approval of the Statement of Accounts by the Audit, Pensions and Standards CommitteeCommittee on 16 September 2014.

Audit differences

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

The final materiality level for this year's audit of the Authority's financial statements was set at £14 million. Audit differences below £550k are not considered significant. In our *External Audit Plan 2013/14*, presented to you in February 2014 we reported our materiality for planning purposes as £22 million equating to approximately 3 percent of gross revenue. In the period leading up to the final accounts audit we reassessed our approach to materiality nationally due to higher risk in the sector as a whole and a number of accounting changes related to pensions and NDR. As a result we reduced materiality for the Authority to £14 million. This equates to around 2 percent of gross revenue.

Our audit identified a total of two significant audit differences, which we set out in Appendix 3. We have reviewed the final version of the financial statements and confirmed that the adjustments identified have been put through appropriately.

The table below illustrate the total impact of audit differences on the Authority's movements on the balance sheet as at 31 March 2014. Due to the revaluation adjustments and transfers to the capital adjustment account, there is no net impact on the general fund balance or usable reserves

Balance Sheet as at 31 March 2014

£m	**Pre-audit (£000)**	**Post-audit (£000)**	***Ref (App.3)***
Property, plant and equipment			
-Council Dwellings	980,065	1,095,964	*1 a*
-Other Land and Buildings	293,083	315,079	*2 a*
Net worth	**1,273,148**	**1,411,043**	
Unusable reserves	784,529	922,423	*1b, 2b*

Proposed opinion and audit differences (continued)

We have identified no issues in the course of the audit of the Fund that are considered to be material.

In addition, we identified a small number of presentational adjustments required to ensure that the accounts are compliant with the *Code of Practice on Local Authority Accounting the United Kingdom 2013/14 ('the Code')*. We have reviewed the final version of the financial statements and confirmed that these presentational adjustments have been put through appropriately.

Pension fund audit

Our audit of the Fund did not identify any material misstatements.

For the audit of the Fund we used a materiality level of £11.4 million. Audit differences below £570k are not considered significant.

We anticipate issuing an unqualified audit opinion following approval of the Statement of Accounts by the Audit, Pensions and Standards Committee on 16 September 2014.

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.

Pension Fund Annual Report

We have reviewed the "London Borough of Hammersmith and Fulham Pension Fund Annual Report 2013/14" and confirmed that:

- it complies with the requirements of the Local Government Pension Scheme (Administration) Regulations 2008 and
- the financial and non-financial information it contains is not inconsistent with the financial information contained in the audited financial statements.

We anticipate issuing an unqualified opinion on the Pension Fund Annual Report at the same time as our opinion on the Statement of Accounts.

Section three

Key financial statements areas of audit focus and audit risks

We have worked with officers throughout the year to discuss specific risks and areas of audit focus.

In our External Audit Plan 2013/14, presented to you in February, we identified the key risks affecting the Authority's and the Fund's 2013/14 financial statements. We have now completed our testing of these areas and set out our evaluation following our substantive work.

Since our External Audit Plan we have identified, and added, National Non-Domestic Rates (NNDR) as a significant risk to the Authority as a result of the implementation of the Business Rates Retention Scheme in 2013/14.

The table below sets out our detailed findings for each of the areas of focus and risks that are relevant to the Authority and Pension Fund.

Additionally, we considered the risk of management override of controls, which is a standard risk for all organisations.

Our controls testing and substantive procedures, including journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual, did not identify any issues.

Area of Focus	Issue	Findings
Cash	Cash has a pervasive impact on the financial statements and provides comfort for other areas of the financial statements. This area of focus affects the Authority.	We have sought external bank confirmations and reviewed the controls over bank reconciliations. We are satisfied that these controls have operated throughout the year and that the cash figure in the financial statements is materially accurate.
Pension Costs and Liabilities	Pension valuations require a significant level of expertise, judgement and estimation and are therefore more susceptible to error. This is also a very complex accounting area increasing the risk of misstatement. This area of focus affects the Authority.	We have confirmed that the pensions costs and liabilities recognised in the accounts were accurately drawn from the report from the actuary. We have reviewed the accounting treatment for associated balances and transactions in order to confirm that it was in line with the requirements of the CIPFA code. We have not identified any issues to report.

Key financial statements areas of audit focus and audit risks (continued)

We have worked with officers throughout the year to discuss specific risks and areas of audit focus.

Area of focus	Issue	Findings
Property, Plant and Equipment	The Authority has a significant asset base primarily relating to Council dwellings and Investment property. The potential for impairment/valuation changes makes this balance inherently risky due to the high level of judgement and estimation uncertainty. This area of focus affects only the Authority.	To seek assurance that property, plant and equipment is reasonably stated we have performed the following audit procedures: • Reviewed management's assessment of property valuations and impairment calculations to gain assurance they are reasonably stated; • Considered the valuer's report and tested to confirm the valuation and accounting entries of the assets valued are correctly stated; • Compared the assumptions made by the valuer to benchmarks for consistency; and • Substantively tested capital additions and disposals for accuracy and completeness. Our work has highlighted three areas to bring to your attention: 1) *Not valuing all assets in the same class on the same basis:* We noted that following a change in valuer the valuation methodology was amended compared to the prior year. The nine schools revalued as part of the Authority revaluation programme incurred significant revaluation losses. The potential impact of revaluing the remaining schools on the amended basis had not been considered. The Authority has since revalued the whole schools portfolio using the new methodology resulting in a revaluation gain of £2.7m. 2) *Valuing PPE at the beginning not the end of the accounting period:* We noted that external valuation reports for dwellings were effective as at 1 April 2013 therefore, given the valuation movements over the year might not reflecting the true market value of dwellings at 31 March 2014. In order to reflect year end property market conditions the Authority has since applied an indexation factor of 12% to dwellings stock. 3) *Excluding capital additions within the revaluation programme:* As per the Authority's policies over revaluations, capital additions are not incorporated within formal revaluations in order to ensure that formal valuations can be completed in time for the production of the financial statements. This presents an inherent assumption that all additions enhance the capital value of the asset whereas this may not be the case. Additions should be incorporated within formal revaluations, however the total level of additions for schools and council dwellings accounts for less than 2% of its year end value which is deemed to be not material. We have raised a recommendation that the revaluation methodology be revisited.

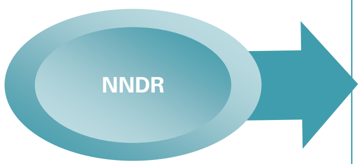
Key financial statements areas of audit focus and audit risks (continued)

We have worked with officers throughout the year to discuss specific risks and areas of audit focus.

Area of focus	Issue	Findings
	During the year, the Pension Fund has undergone a triennial valuation with an effective date of 31 March 2013 in line with the Local Government Pension Scheme (Administration) Regulations 2008. The share of pensions assets and liabilities for each admitted body is determined in detail, and a large volume of data is provided to the actuary to support this triennial valuation. The IAS 19 numbers to be included in the financial statements for 2013/14 has been based on the output of the triennial valuation rolled forward to 31 March 2014. For 2014/15 and 2015/16 the actuary will then roll forward the valuation for accounting purposes based on more limited data. There is a risk that the data provided to the actuary for the valuation exercise is inaccurate and that these inaccuracies affect the actuarial figures in the accounts. This area of focus also impacts the Pension Fund.	We reviewed the data provided to the actuary and confirmed that it was consistent with underlying records. We did not identify any issues to report.

Key financial statements areas of audit focus and audit risks (continued)

Since the audit plan we have identified one specific audit risk for the Authority.

Key audit risk	Issue	Findings
	Due to the introduction of Business Rate Localisation, with effect from 1st April 2013, there were significant changes in the requirements for the disclosure of NDR balances and transactions, as per the CIPFA Code. Furthermore, there were significant variances in the balance sheet and the CIES as a result of the change of accounting treatment. These factors meant that non-domestic rates were reassessed as a significant risk area for the audit and therefore have been included as a key financial statement audit risk.	No issues were identified from testing performed

Accounts production and audit process

The Authority has good processes in place for the production of the accounts and good quality supporting working papers.

Officers dealt efficiently with audit queries and the audit process could be completed within the planned timescales.

The Authority has implemented all but one of the recommendations in our *2012/13 ISA 260 Report*.

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 has good financial reporting arrangements in place. In particular it is noted officers have identified technical or subjective areas throughout the year and liaised with us to consider the implications for financial reporting. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 30 June 2014.
Quality of supporting working papers	Our *Accounts Audit Protocol*, which we issued on 3 March 2014 and discussed with Chris Harris (Head of Corporate Accountancy) and Maria Campagna (Finance Manager – Closing & Accountancy) set out our working paper requirements for the audit. The quality of working papers provided was high and met the standards specified in our *Accounts Audit Protocol*.
Response to audit queries	Officers resolved all audit queries in a reasonable time

Element	Commentary
Pension fund audit	The audit of the Fund was completed alongside the main audit. There are no specific matters to bring to your attention relating to this.

Prior year recommendations

As part of our audit we have specifically followed up the Authority's progress in addressing the recommendations in last years ISA 260 report.

The Authority has implemented all but one of the recommendations in our *ISA 260 Report 2012/13*. As a result of the postponement of implementing Tri-Borough managed services to April 2015, the Authority has not yet included a fixed asset register module within their finance system.

Appendix 2 provides further details.

Control environment

The Council's organisational and control environment is effective, and controls over the key financial systems are sound.

During February 2014 we completed our control evaluation work. We did not issue an interim report as there were no significant issues arising from this work. For completeness we outline our key findings from this work.

Organisational control environment

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit.

We obtain an understanding of the Authority's overall control environment and determine if appropriate controls have been implemented. We do not complete detailed testing of these controls.

We consider that your organisational controls are effective overall.

Controls over key financial systems

We review the outcome of internal audit's work on the financial systems to influence our assessment of the overall control environment, which is a key factor when determining the external audit strategy.

We also work with your internal auditors to update our understanding of some of the Authority's key financial processes where these are relevant to our final accounts audit.

Where we have determined that this is the most efficient audit approach to take, we test selected controls that address key risks within these systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Our assessment of a system will not always be in line with your internal auditors' opinion on that system. This is because we are solely interested in whether our audit risks are mitigated through effective controls, i.e. whether the system is likely to produce materially reliable figures for inclusion in the 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 and the Fund'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 London Borough of Hammersmith and Fulham and Hammersmith and Fulham Pension Fund for the year ending 31 March 2014, we confirm that there were no relationships between KPMG LLP and London Borough of Hammersmith and Fulham and Hammersmith and Fulham Pension Fund, 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 Audit Commission's 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 Executive Director of Finance and Corporate Governance for presentation to the Audit, Pensions 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 party, public interest reporting, questions/objections, opening balances etc).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2013/14 financial statements.

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 the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

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 have not identified any significant risks to our VFM conclusion, but we considered the delivery of savings plans as an area of audit focus.

Key findings

Overleaf we set out the findings in respect of those areas where we have identified as an area of audit focus for our VFM conclusion.

We concluded that we did not need to carry out additional work for these risks as there was sufficient relevant work that had completed by the Authority, other inspectorates and review agencies in relation to these risk areas.

Significant Matters

We did not identify any specific VfM risks but we considered the delivery of savings plans as an area of audit focus.

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

VfM Audit focus	Risk description and link to VFM conclusion	Assessment
	Based on the current plan, which covers the period 2013/14 to 2015/16, there is a significant savings requirement over the three year period in the region of £65m. The savings required for 2013/14 of £21.4m have been identified and early indications – including the 2012/13 achievements and under-spends are positive. The pressure mounts considerably in 2014/15 when there is a further £18m saving requirement and 2015/16 when an additional £24.5m needs to be found. Many of these savings requirements are due to be delivered via the Tri borough working arrangements. However, finding additional savings year after year will be a challenge. The Authority will need to establish and manage its savings plans to secure longer term financial and operational sustainability and ensure that any related liabilities are accounted for in its 2013/14 financial statements as appropriate.	Our main accounts work has confirmed that the Authority has met its £21.4m savings targets for 2013/14. As part of our Value for Money work we have reviewed the Authority's processes for delivery of its savings plans and consider that robust, achievable plans are in place. The Authority has a current medium term financial plan in place which gives due consideration to potential funding reductions. Based on its assumptions there will be further funding reductions of £18m in 2014/15, £25m in 2015/16 and £10m in 2016/17. Service level savings plans have been identified and are being monitored for 2014/15. The Authority is refreshing its medium term financial plan. Detailed proposals are to be presented to Cabinet in the autumn with the objective of agreeing a three year budget – for 2015/16 to 2017/18 .

Conclusion

We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

VFM criterion	Met
Securing financial resilience	✓
Securing economy, efficiency and effectiveness	✓

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 do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸ ***Priority three***: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
1	❷	**Valuation Methodology** As noted on page 7 three issues were identified in relation to the Authority's approach to the year end valuation of PPE. There is a risk that the Council's current revaluation methodology does not comply with *the Code*. There are three points of improvement to be considered: 1. The date at which the valuation is performed and need to ensure any subsequent movements are considered. 2. The consistency of the valuation of a class of asset where the valuation methodology is updated. 3. The inclusion of current year capital additions as part of the valuation programme. **Recommendation** We recommend that the methodology in the above areas is revisited and changes adopted ahead of the next reporting period.	The recommendation is agreed. The methodology for valuing PPE will be reviewed and changes adopted, as appropriate, ahead of the next reporting period. Any change to the methodology will be developed in concert with the Council's internal and external valuers. The Council will also consult with External Audit concerning any change. Bi-Borough Director of Finance, December 2014

Appendix 2: Follow up of prior year recommendations

The Authority has implemented all but one of the recommendations in our *ISA 260 Report 2012/13.*

This appendix summarises the progress made to implement the recommendations identified in our *ISA 260 Report 2012/13* and re-iterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	2
Implemented in year or superseded	1
Remain outstanding	1

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at July 2014
1	2	**Non-Current Asset Management** The Authority has over 14,000 assets with a value of approx £1.35bn which are controlled and utilised by departments and divisions across the Council. An asset base of this scale and diversity poses a number of challenges, both from a technical perspective with differences in valuation treatments and in terms of maintaining up to date records. The Authority currently uses a number of spreadsheets as its asset database and to perform the required accounting calculations. This relies on a number of manual calculations and is both time consuming throughout the year and places significant time pressures of the Capital team during the year end closedown process. The Authority should consider implementing an asset management system with the required functionality to improve efficiency of officers throughout the year and increase accuracy in the financial reporting process reducing the risk of error.	Bi-Borough Director of Finance, April 2014	**Not Implemented** An asset management system is due to be implemented as part of the transition towards Tri-Borough managed services, which was originally planned for September 2014 but is now scheduled for April 2015.

Appendix 2: Follow up of prior year recommendations

The Authority has implemented all but one of the recommendations in our *ISA 260 Report 2012/13.*

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at July 2014
2	3	**Investments** The Authority has an active treasury management function placing a number of investments throughout the year for significant sums. Our review of the control environment found it to be operating effectively and as designed with segregation of duties and a defined authorisation process for each investment placed. For individual investments over £10m the Council has an additional layer of approval, which requires review/authorisation by a third officer. Of the 12 investments greater than £10m tested within our sample we identified two that did not have the additional level of authorisation. Although the control had not been performed, we noted no issues indicating the investments were otherwise outside the Authority's policy. Whilst this represents a strong control environment, there is an opportunity to remove this additional layer of approval, to make the process more efficient and reducing the time officers spend processing each investment. A preparer and reviewer is sufficient to segregate duties and mitigate the risk of error and fraud.	Director of Corporate Finance & Investment, September 2013	**Implemented** Investments over £10m now requires review/authorisation by only two finance officers. We observed this segregation of duties through conducting walkthroughs of the investment approval process.

Appendix 3: Audit differences

This appendix sets out the significant audit differences.

For the Authority audit we are reporting all significant audit differences over £550k.

We have confirmed that the final revised set of accounts includes these adjustments.

There are no unadjusted audit differences.

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit, Pensions and Standards Committee). There are no uncorrected audit differences to report. We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

Corrected audit differences – Authority

The following table sets out the significant audit differences identified by our audit of London Borough of Hammersmith and Fulham financial statements for the year ended 31 March 2014.

	Impact					
No.	**Income and Expenditure Statement**	**Movement in Reserves Statement**	**Assets**	**Liabilities**	**Reserves**	**Basis of audit difference**
1a	Cr HRA expenditure £99,668k		Dr Council Dwellings £115,899k		Cr Surplus on revaluation of Property Plant and Equipment Assets £16,231k	In the first draft of the financial statements, revaluation gains for HRA dwellings were effective as at 1 April 2013 as per valuation reports. In order to bring valuations in line with the balance sheet date an indexation factor of 12% has been applied on the net book value to reflect movements in the property market during 13/14. We benchmarked this indexation factor against third party research and consider this factor to be reasonable. This has resulted in a revaluation gain of £116m. The movement between the revaluation reserve and the CIES is in order to reverse previous years impairments within HRA dwellings assets.
1b		Dr HRA £99,668k			Cr Capital Adjustment Account £99,668k	The transfer is required to move HRA gains into the capital adjustment account in order to neutralise the effects on the CIES.

Appendix 3: Audit differences

This appendix sets out the significant audit differences.

For the Authority audit we are reporting all significant audit differences over £550k.

We have confirmed that the final revised set of accounts includes these adjustments.

There are no unadjusted audit differences.

	Impact					
No.	**Income and Expenditure Statement**	**Movement in Reserves Statement**	**Assets**	**Liabilities**	**Reserves**	**Basis of audit difference**
2a	Cr Childrens Services Expenditure £20,418k		Dr Other Land and Buildings £21,996k		Cr Surplus on revaluation of Property Plant and Equipment Assets £1,578k	In the first draft of the financial statements the revalued schools had been valued on a different basis to the prior year. The adjustments reflects the revaluation of the remaining schools on the same basis following formal revaluation of all schools. We have confirmed the revised revaluations and gain back to valuers reports.
2b		Dr General Fund £20,418k			Cr Capital Adjustment Account £20,418k	This is the transfer from the general fund to the capital adjustment account in order to neutralise the effect of revised schools revaluations on the CIES.
	Cr £120,086	**Dr £120,086**	**Dr £137,894k**	**-**	**Cr 137,894k**	**Total impact of adjustments**

Appendix 4: Declaration of independence and objectivity

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

Requirements

Auditors appointed by the Audit Commission 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 Audit Commission's *Standing Guidance for Local Government Auditors* ('Audit Commission 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. Audit Commission 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 Audit, Pensions and Standards 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 (continued)

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 the London Borough of Hammersmith and Fulham and Hammersmith and Fulham Pension Fund or the financial year ending 31 March 2014, we confirm that there were no relationships between KPMG LLP and London Borough of Hammersmith and Fulham and Hammersmith and Fulham Pension Fund , 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 Audit Commission's requirements in relation to independence and objectivity.

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