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

North London Waste Authority

FINAL

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 Philip Johnstone, 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 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 North London Waste Authority ('the Authority') in relation to the Authority's 2013/14 financial statements; and
- the work to support our 2013/14 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 2013/14*, presented to you in June 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 August 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; and
- considering the results of any relevant work by the Authority and other inspectorates and review agencies in relation to these risk areas.

However, as set out in our Audit Plan, following the Authority's decision not to proceed with the procurement process being followed for a Waste Service Contract and a Fuel Use Contract , a review of the procurement process is required in order to meet our VFM conclusion responsibilities.

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.
- Section 4 outlines our key findings from our work on the VFM conclusion.

Our recommendations are included in Appendix 1.

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. 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.
Audit adjustments	During the audit the Authority identified one material adjustment to be made to the draft financial statements. This is in relation to the change in status of the contingent liability that was disclosed initially and has resulted in an increase in expenditure and short term creditors by £5,000,000. We provide further information on this adjusted difference in Appendix 2. The Authority made a small number of non-trivial adjustments, most of which were of a presentational nature. There was no impact on the General Fund. The group financial statements incorporate one unadjusted error originally reported to LondonWaste Limited (LWL) by its auditors, BDO. The effect of this unadjusted error is to decrease the group's surplus by £140,000 and decrease the net assets of the group by £140,000. We provide further information on this unadjusted misstatement in Appendix 2. We also seek specific management representations that the effect of this unadjusted misstatement is immaterial. We have provided a template to the Head of Finance for presentation to the Authority. We require a signed copy of your management representations before we issue our audit opinion. We have raised one recommendation arising from our work, detailed in Appendix 1.
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 has been completed within the planned timescales. We have worked with Officers throughout the year to discuss the specific risk areas for this year's audit. The Authority addressed the issues appropriately.
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. 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.
VFM conclusion and risk areas	Following the Authority's decision not to proceed with the procurement process being followed for a Waste Service Contract and a Fuel Use Contract , a review of the procurement process is required in order to meet our VFM conclusion responsibilities. The Authority has only recently finalised the matters arising from the decision to stop the procurement. Consequently, we have only recently started our review of the procurement process. We will therefore not be in a position to conclude about the Authority's arrangements relating to VFM by 30 September 2014.
Certificate	We cannot issue a certificate and close the audit because of ongoing correspondence with local government electors and the work we need to complete to review the Authority's procurement processes for the Waste Services and Fuel Use contracts that were stopped during the year. We will update Members through our progress reports on further developments but there are no matters under discussion that we consider materially affect our audit opinion.

Proposed opinion and audit differences

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

We anticipate issuing an unqualified audit opinion in relation to the Authority's financial statements by 30 September 2014.

The wording of your Annual Governance Statement accords with our understanding.

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 Board on 29 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.

During the audit the Authority identified one material adjustment which has been reflected in the final draft of the financial statements. This adjustment has been caused by the:

- Change in status of the contingent liability disclosed initially which is now recognised as a year end creditor of £5,000,000. This was due to the Authority reaching agreement with the other parties in July about the amount of the Authority's liability.

The audit of LWL's accounts identified one unadjusted audit difference. LWL's auditors, BDO, reported this difference to LWL's Board in May 2014.

The Authority has not adjusted its financial statements for this audit difference on consolidation and so it is present within the Authority's group financial statements. We bring this to your attention to help you in fulfilling your governance responsibilities. This audit difference is:

- An overcharge of £140,000 depreciation against the property, plant and equipment balance.

The effect of this unadjusted error is to decrease the group's surplus by £140,000 and decrease the net assets of the group by £140,000. We have discussed this with management, who have declined to amend the group accounts so as to maintain consistency with LWL's published financial statements and due to the materiality of the balance in question. Management also considered the amount of LWL finance resource that would be required to amend the LWL asset register in order to make the required changes was not cost effective. We will seek specific management representations that the effect of this unadjusted misstatement is immaterial.

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 understand that the Authority will be addressing these where significant.

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.

Accounts production and audit process

The Authority has sound 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.

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. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 30 June 2014. The Authority identified and made one material adjustment to this draft during the audit. This was in line with our understanding and supported by appropriate audit evidence.
Quality of supporting working papers	The Authority's working papers prepared by the Finance team to support the financial statements were of a high quality. This had a positive impact on the audit as it helped to ensure an efficient audit.
Response to audit queries	Officers resolved all audit queries in a reasonable time. This ensured that the audit was completed efficiently and within agreed timescales.

Element	Commentary
Group audit	To gain assurance over the Authority's group accounts, we placed reliance on work completed by BDO on the financial statements of LWL. The group financial statements contain one unadjusted error originally reported to LWL by BDO, detailed in Appendix 2. We seek management representations that the effect of these unadjusted misstatements in the group accounts is immaterial.

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 North London Waste Authority for the year ending 31 March 2014, we confirm that there were no relationships between KPMG LLP and North London Waste Authority, 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 Head of Finance for presentation to the Authority. We require a signed copy of your management representations before we issue our audit opinion.

As noted above, the letter asks for specific representations on the uncorrected audit adjustments included in the group accounts.

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 need to review the Authority's decision not to proceed with its major procurement process to enable us to reach a conclusion about the Authority's arrangements to secure VFM.

As this review has only just started we are not yet is a position to conclude whether 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.

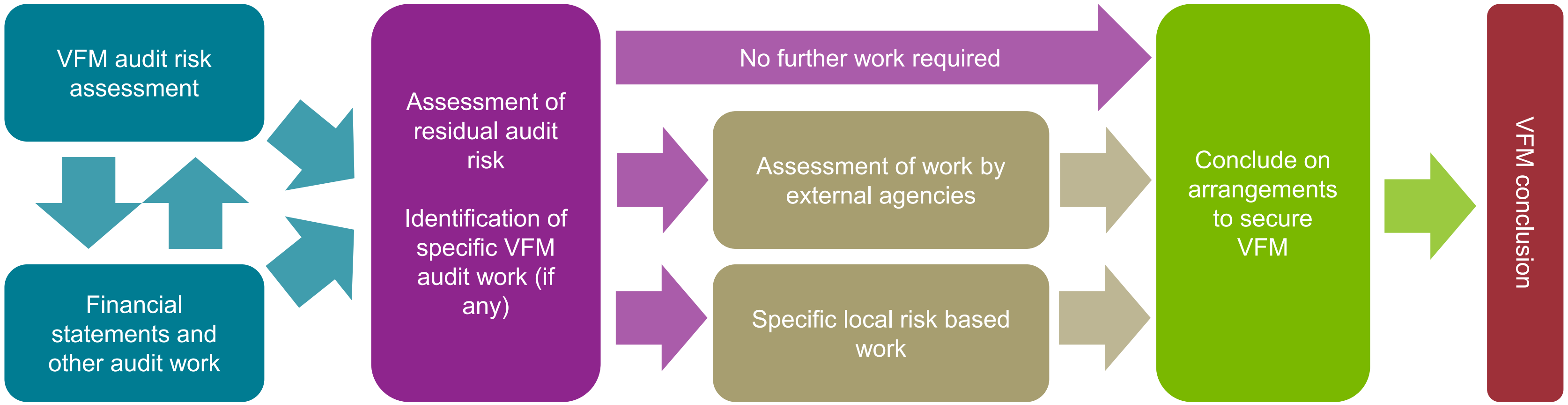
The key elements of the VFM audit approach are summarised in the diagram below.

Work to be done

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

Following the Authority's decision not to proceed with the procurement process being followed for a Waste Service Contract and a Fuel Use Contract, a review of the procurement process is required in order to meet our VFM conclusion responsibilities. The Authority has only recently finalised the matters arising from the decision to stop the procurement.

Consequently, we have only recently started our review of the procurement process. We will therefore not be in a position to conclude about the Authority's arrangements relating to VFM by 30 September 2014.



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	❸	**Landfill Tax expenditure supporting documentation** The Authority currently pay £900,000 per month on account to LondonWaste Limited in respect of Landfill Tax expenditure. During the audit we were unable to review a contract or formal documentation supporting the value of this expenditure. We note that final agreement of any outstanding balance is completed after the year end to ensure an accurate final balance is recorded in the financial statements and accounting records. The Authority should ensure formal documentation is available for review regarding all expenditure, to ensure a robust and appropriate audit trail.	**Agreed** The Authority's actual LFT liability is determined at year-end but because of the scale of the amount payable (c. £11m in 2013/14) the Authority makes a monthly payment on account to LondonWaste Ltd based upon the estimated liability. Any under or overpayments are paid by or refunded to the Authority once the final liability is determined. Having regard to forecast tonnages that would attract a LFT charge and the increase in the LFT rate from £64 to £72 per tonne in 2013/14, LondonWaste Ltd and the Authority agreed that the monthly payment on account should be increased from £0.8m to £0.9m. Each party acted upon the agreement, LondonWaste increased its monthly invoice to the Authority and were paid by the Authority. It is the norm for these arrangements to be recorded in writing but not on this occasion. This was an omission and officers will take steps to ensure that best practice is followed in future. **Head of Finance** **Immediate**

Appendix 2: Audit differences

This appendix sets out the significant 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 the Authority's case is the Board). 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

During our audit the Authority identified one material adjustment to be made to the draft 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**
1	Dr Environmental and Regulatory Services £5,000k			Cr Short Term Creditors £5,000k		**Short Term Creditor** This adjustment recognises the change in status of the contingent liability disclosed initially to being expenditure and a year end creditor.
	Dr £5,000k	**-**	**-**	**Cr £5,000k**	**-**	**Total impact of adjustments**

Uncorrected audit differences

We identified no errors in the financial statements of the Authority that management did not correct. BDO identified the following misstatements during their audit of LWL. The Authority has not adjusted the financial statements on consolidation and so the errors are present within the Authority's group 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**
1	Cr Environmental and Regulatory Services £140k		Dr Property, Plant and Equipment £140k			**Depreciation Charge** This audit difference recognises a higher than required depreciation charge made in the year.
	Cr £140k	**-**	**Dr £140k**		**-**	**Total impact of adjustments**

Appendix 3: 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 Board.

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 3: 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 North London Waste Authority for the financial year ending 31 March 2014, we confirm that there were no relationships between KPMG LLP and North London Waste Authority, 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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