External Audit Report 2017/18

London Borough of Hackney

—

July 2018

Content

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This report is addressed to the London Borough of Hackney (the Authority) and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. PSAA issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on PSAA's website (www.psaa.co.uk).

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

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

Important notice

This report is presented in accordance with our PSAA engagement. Circulation of this report is restricted. The content of this report is based solely on the procedures necessary for our audit. This report is addressed to the London Borough of Hackney (the Authority) and has been prepared for your use only. We accept no responsibility towards any member of staff acting on their own, or to any third parties. The National Audit Office (NAO) has issued a document entitled Code of Audit Practice (the Code). This summarises where the responsibilities of auditors begin and end and what is expected from the Authority. External auditors do not act as a substitute for the Authority's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

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

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

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

Status of our audit: Our audit is not yet complete and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status of our audit at the Audit Committee meeting. The following work is ongoing:

- **Financial statements audit and pension fund:** Finalisation of our work on payroll, collection fund, final audit procedures on the pension fund annual report and updated accounts.
- **Whole of Government accounts pack:** Work ongoing.
- **Elector queries:** We have one elector query in relation to 2016/17, where work is ongoing.

Summary

Financial statements audit – see section 2 for further details
Subject to all outstanding queries and procedures being satisfactorily resolved we intend to issue an unqualified audit opinion on the Authority's financial statements for the deadline of 31 July 2018, following the Audit Committee adopting them and receipt of the management representations letter.

Financial statements audit – see section 2 for further details

Subject to all outstanding queries and procedures being satisfactorily resolved we intend to issue an unqualified audit opinion on the Authority's financial statements for the deadline of 31 July 2018, following the Audit Committee adopting them and receipt of the management representations letter.

We also anticipate issuing an unqualified audit opinion in relation to the Pension Fund's financial statements for the deadline of 31 July 2018.

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

- There is one unadjusted difference in relation to indexation applied to PPE. Further details on this are in Appendix 3.
- We agreed presentational changes to the accounts with Finance, mainly related to compliance with the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2017/18.
- We are requesting the routine management requests which are consistent with those requested in previous years.
- We will report that your AGS complies with delivering Good Governance guidance issued by CIPFA / SOLACE in April 2016.
- We did not receive any queries or objections from local electors in 2017/18, however have one elector query remaining from 2016/17.

We are now in the completion stage of the audit and anticipate issuing our audit opinion on 31 July 2018. We also intend to issue our 2017/18 Annual Audit Letter in August/September 2018.

Value for money – see section 3 for further details

Based on the findings of our work, we have concluded that the Authority has adequate arrangements to secure economy, efficiency and effectiveness in its use of resources. We therefore anticipate issuing an unqualified value for money conclusion for the deadline of 31 July 2018.

Summary

Other matters

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

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

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

We have not identified any matters that would require us to issue a public interest report. In addition, we have not had to exercise any other audit powers under the Local Audit & Accountability Act 2014

There are no other matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2017/18 financial statements.

There were no recommendations raised in the prior year. We have made 2 new recommendations as a result of our 2017/18 work. The recommendations relates to the accuracy of membership data provided to Equiniti by the Authorities HR team and the payment of untaken leave on contract termination. All recommendations are shown in appendix 1.

We undertake other grants and claims work for the Authority that does not fall under the PSAA arrangements. The status of our grants and claim work is summarised below:

- Teachers Pensions: The reporting accountant assurance deadline is the 30 November 2018. We will complete the fieldwork in relation to this in October 2018;
- Pooling of Housing Receipts: The reporting accountant assurance deadline is the 30 November 2018. We will complete the fieldwork in relation to this in October 2018; and
- Housing Benefits: The reporting accountant assurance deadline is the 30 November 2018. We will complete the fieldwork in relation to this in August and September 2018.
- Education and Skills Funding Agency Subcontractor Grant Claim: The reporting accountant assurance deadline is the 14 September 2018. We will complete the fieldwork in relation to this in August and September 2018.

The fees for this work is explained in section two.

Financial statements audit

We audit your financial statements by undertaking the following:

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

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

1. Business understanding	In our 2017/18 audit plan we assessed your operations to identify significant issues that might have a financial statements consequence. We confirmed this risk assessment as part of our audit work. We provide an update on each of the risks identified later in this section.
2. Assessment of the control environment	We assessed the effectiveness of your key financial system controls that prevent and detect material fraud and error. We found that the financial controls on which we seek to place reliance are operating effectively. We reviewed work undertaken by your internal auditors, in accordance with ISA 610 and used the findings to inform our work. We have chosen not to place reliance on their work due to the approach we adopted for the financial statements audit.
3. Prepared by client request (PBC)	We produced the PBC to summarise the working papers and evidence we ask you to collate as part of the preparation of the financial statements. We discussed and tailored our request with the Chief Accountant and this was issued as a final document to the finance team. We are pleased to report that this has resulted in generally good-quality working papers with clear audit trails maintained on the KPMG secure database. Minor areas for refinement were noted and discussed with the finance team.

Financial statements audit

4. Accounts Production	We received complete draft accounts on 31 May 2018, in line with the publication deadline. The accounting policies, accounting estimates and financial statement disclosures are in line with the requirements of the Code of Practice on Local Authority Accounting in the United Kingdom 2017/18. The Authority incorporated measures into its closedown plan to manage this complex process. The Authority recognised the additional pressures which the earlier closedown brought and we engaged with officers in the period leading up to yearend to proactively address issues as they emerged. We consider that the overall process for the preparation of your financial statements is adequate. We would highlight that as the timetable for the accounts production tightens, increased scrutiny and documentation around areas requiring estimate and any change at the year end, should be documented. We thank Finance for their cooperation throughout the visit which allowed the audit to progress and complete within the allocated timeframe.
5. Testing	We have summarised the findings from our testing of significant risks and areas of judgement in the financial statements on the following pages. During the audit we identified presentational issues which have been adjusted, none had a material impact on the outturn position detailed within the financial statements.
6. Representations	You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We provided a draft of this representation letter to the Group Director - Finance and Corporate Resources on 11 July 2018. We draw attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us.

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

— Significant difficulties encountered during the audit;

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

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

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

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2017/18 financial statements.

To ensure that we provide a comprehensive summary of our work, we have over the next pages set out:

- The results of the procedures we performed over the valuation of land and buildings, the valuation of the pension liability, managed services operation and faster close which were identified as significant risks within our audit plan and which will form a part of our audit opinion;
- The results of our procedures to review the required risks of the fraudulent risk of revenue recognition and management override of control; and
- Our view of the level of prudence applied to key balances in the financial statements.

Financial statements audit

Authority significant audit risks

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

SIGNIFICANT audit risk	Account balances effected	Summary of findings
Valuation of land and buildings The Authority held land and buildings with a value of £4,404 million at 31 March 2017. The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Authority has adopted a rolling revaluation model which sees land and buildings revalued over a five year cycle unless itis thought that the value may have changed materially where they are revalued more frequently. As a result individual assets may not be revalued for four years. This creates a risk that the carrying value of those assets not revalued in year differs materially from the year end fair value.	**Note 13: PPE** £4,130 million PY £4,004 million (NBV)	As noted opposite the Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Authority has adopted a rolling revaluation model which sees all land and buildings revalued over a five year cycle. As a result of this, however, individual assets may not be revalued for four years. This creates a risk that the carrying value of those assets not revalued in year differs materially from the year end fair value. In addition, as the valuation is undertaken as at 1 April, there is a risk that the fair value is different at the year end. We have: • reviewed the approach that the Authority adopted to assess the risk that assets not subject to valuation were materially misstated and considered the robustness of that approach; • reviewed management's assessment of property valuations and impairment calculations; • confirmed the information provided to the in house valuer from the Authority; • compared the assumptions made by your valuer to benchmarks and to the assumptions used for 2016/17 for consistency; • completed testing over new capital additions in year to confirm these are appropriately capitalised and that Authority ownership is evidenced; and • reviewed disposals made in year and confirm appropriate removal from the PPE balance in 2017/18. **We have noted one unadjusted and one adjusted difference in relation to the application of PPE indexation. This is detailed within Appendix 3.**

Financial statements audit

SIGNIFICANT audit risk	Account balances effected	Summary of findings
Pension: Valuation of assets and liabilities The net pension liability at 31 March 2018 of £685 million represents a material element of the Authority's balance sheet. The Authority is an admitted body of the London Borough of Hackney Pension Fund, which had its last triennial valuation completed as at 31 March 2016. This forms an integral basis of the valuation as at 31 March 2018. Valuation of the Local Government Pension Scheme relies on assumptions, most notably actuarial assumptions, and actuarial methodology which results in the Authority's overall valuation. There are financial assumptions and demographic assumptions used in the calculation of the Authority's valuation, such as the discount rate, inflation rates, mortality rates etc. Assumptions should reflect the profile of the Authority's employees and should be based on appropriate data. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes. There is a risk that the assumptions and methodology used in the valuation of the Authority's pension obligation are not reasonable. This could have a material impact to net pension liability accounted for in the financial statements.	**Note 44: Defined Benefit Pension Scheme** £685 million Pension Fund Liability. PY: £715 million relates to the Pension Fund Liability.	The fund had its last triennial valuation completed as at 31 March 2016. This forms an integral basis of the valuation as at 31 March 2018. The valuation of the Local Government Pension Scheme relies on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the Authority's overall valuation. There are financial assumptions and demographic assumptions used in the calculation of the Authority's valuation, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Authority's employees, and should be based on appropriate data. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes. There is a risk that the assumptions and methodology used in the valuation of the Authority's pension obligation are not reasonable. This could have a material impact to net pension liability accounted for in the financial statements. As part of our work we reviewed the controls that the Authority has in place over the information sent to the Scheme Actuary, including the Authority's process and controls with respect to the assumptions used in the valuation. We also evaluated the competency, objectivity and independence of the external actuary. We reviewed the appropriateness of the key assumptions included within the valuation and compared them to expected ranges. We involved a KPMG Actuary to provide a specialist assessment of those assumptions, who concluded that overall, the assumptions inherent within the valuation were balanced. In addition, we reviewed the overall Actuarial valuation and considered the disclosure implications in the financial statements. In order to determine whether the net pension liability has been appropriately accounted for we also considered the valuation of pension assets. As part of our audit of the Pension Fund we gained assurance over the overall value of fund assets. We then liaised with the actuary to understand how these assets are allocated across participating bodies and reperformed this allocation. **We have noted an adjusted difference in relation to the application of actual return on assets, together with minor presentational changes to note 44, defined benefit pension schemes.**

Financial statements audit

Authority other areas of audit focus

Those risks with less likelihood of giving rise to a material error but which are nevertheless worthy of audit understanding.

Other areas of audit focus	Account balances effected	Summary of findings
Note 21: NNDR appeals provision	£5 million PY £3 million	The Authority use an independent body to calculate the appeals provision. We have: • gained an understanding over controls related to business rates income and specifically the appeals process; • reviewed the methodology applied in determining the appeal provision including whether this reflects a balanced, cautious or optimistic assessment; and • ensured the report is complete by agreeing data back the Valuation Office Agency (VOA) data. **There are no issues that we need to bring to your attention.**
Note 37: Conditional grant income	£630 million PY £627 million	We have: • reviewed the controls in place to ensure that grants are recognised only when there is reasonable assurance that the Authority will comply with any conditions attached to the grant; • ensured for a sample of grants, that they have been applied over the period necessary to match them with the related costs, for which they are intended to compensate, on a systematic basis; and • ensured that the accounting policy adopted for grants, including method of balance sheet presentation, nature and extent of grants recognised in the financial statements and any unfulfilled conditions and contingencies attached to recognised grants has been disclosed within the accounts. **There are no issues that we need to bring to your attention.**
Note 28. Employee Expenses	£209 million PY £218 million	We have: • tested reconciliations for gross pay and deductions (e.g. pensions, tax and national insurance); and • Substantively tested the payroll balance using statistical sampling. We statistically tested basis pay, agency pay, starters and leavers and key controls surrounding deductions. **No issues were noted as a result of these procedures.**

Financial statements audit

Other areas of audit focus	Account balances effected	Summary of findings
Note 19: Cash & cash equivalents	£71 million PY: £68 million	We have: • reviewed the year end bank reconciliation; • confirmed cash balances with external third parties; and • reviewed, on a sample basis, school cash balances held by the Authority. **There are no issues that we need to bring to your attention.**
Note 28B Non-Payroll Expenditure **Note 22: Short term creditor**	£1,183 million PY: £930 million £155 million PY: £112 million	We have: • agreed a statistical sample of non pay expenditure to third party documentation to confirm classification per the Code; • undertaken cut-off testing, whereby we test a sample of transactions in the period between the 31 March 2018 and the ledger close to ensure these are recorded in the correct period; and • statistically selected a sample of short term creditors and confirmed classification to source documentation. **There are no issues that we need to bring to your attention.**
HRA: HRA Rental Income and Repairs and Maintenance and Management Expenditure	£44 million PY: R&M £39 million £40 million PY: S&M: £38 million	We have: • gained an understanding over controls related to HRA expenditure; and • completed substantive analytical review of expenditures. We have also linked our work to that over payroll and non-payroll expenditure. **There are no issues that we need to bring to your attention.**

Financial statements audit

Pension Fund significant audit risks

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

SIGNIFICANT audit risk	Account balances effected	Summary of findings
Pension Fund Net Asset Statement Valuation of hard to price investments	Net assets: £1,475 million PY: £1,391 million	The Pension Fund invests in a wide range of assets and investment funds, some of which are inherently harder to value or do not have publicly available quoted prices, requiring professional judgement or assumptions to be made at year end. The pricing of complex investment assets may also be susceptible to pricing variances given the number of assumptions underlying the valuation. In the prior year financial statements, £154k out of a total of £1,397 million of investments (less than 1%), were in this harder to price category. For year ended 31 March 2018, £138k out of a total of £1,487 million of investments (less than 1%) were in this harder to price category. As part of our audit of the Pension Fund, we independently verified a selection of investment asset prices to third party information and obtained independent confirmation on asset existence. We also tested the extent to which the Pension Fund had challenged the valuations reported by investment managers for harder to price investments and obtained independent assessment of the figures. **There are no issues that we need to bring to your attention.**

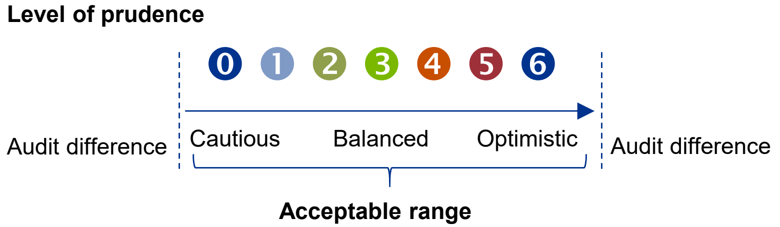
Financial statements audit

Risks that ISAs require us to assess in all cases	Why	Our findings from the audit
Fraud risk from revenue recognition **Authority & Pension Fund**	Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. We do not consider this to be a significant risk for the majority of the Authority's and Pension Fund income as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebut this risk for council tax, business rates, housing rents, annual central government grants, social services income and pension fund contributions and do not incorporate specific work into our audit plan in these areas over and above our standard fraud procedures. However, we do consider it for income relating to s106 monies that span financial years and often have to be used on specific projects.	For other income, we obtained a breakdown of Cost of Services and removed Grant income credited to services. We removed the conditional grant element and tested this as below: • We classified conditional grant income as an area of audit focus for 2017/18 and have outlined above the audit work we undertook which also fulfilled our responsibilities for this objective. Other income was tested as an other account within our audit work. • Other areas of income, for example taxation and precepts were tested for completeness. **There are no matters arising from this work that we need to bring to your attention.**
Fraud risk from management override of controls **Authority & Pension Fund**	Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry 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. We have not identified any specific additional risks of management override relating to this audit.	Our procedures, including testing of journal entries, accounting estimates and significant transactions outside the normal course of business, no instances of fraud were identified. We have performed specific procedures to: • review accounting judgements which are impacting the reported outturn position; • review of controls associated with, and undertaken, sample testing of manual journals; • reconciled the year end performance to in year financial report to ensure that divergence in performance can be understood and justified; and • reviewed the year end cut off process to ensure that revenue and expenditure items have been reflected within the correct period. **There are no matters arising from this work that we need to bring to your attention.**

Financial statements audit

Judgements in your financial statements

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



Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Note 21: NNDR provisions	3	3	£5.4M (PY:£3M)	In 2013/14, local authority funding arrangements meant that the Authority is now responsible for a proportion of successful rateable value appeals. The Authority use an external specialist 'Analyse Local' to inform their NNDR appeals provision. The Authority provides for a fixed percentage of outstanding appeals in accounting for the potential liability, based on historical appeals success rates. Based on the above work, we believe the Authority has represented a balanced view of provisions, within the acceptable range of estimates.
Note 13: PPE Valuation	3	3	£4,343M (PY:£4,208M)	PPE have been subject to a revaluation in the year. Typically, the Authority completes a rolling plan of revaluations, with 20% revalued annually at 1 April with the remaining 80% indexed. All assets are then indexed to 31 March. In 2017/18, an estimated indexation was applied for Q4. This was then compared to actual indexation following their publication in July 2018. This identified a material difference in the valuation of the assets of £20.6m (uplift) across all assets held by the Council. £18.5m of the variance related to HRA assets and was adjusted. This has been adjusted within the updated financial statements. The remainder was not adjusted. Appendix 3 provides more information on this. Based on the above work, and subject to the above adjustment, we believe the Authority has a balanced view of PPE valuations.

Financial statements audit

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Note 13: PPE: Infrastructure assets (Depreciation)	4	n/a	£10M (PY:£9.4M)	We have reviewed the depreciation charged to each class of assets. For infrastructure assets, we noted that the depreciation charge was less than we would have expected. Further investigation identified that this was a result of a historic system fault which had previously overcharged depreciation. To ensure that the depreciation charged was a reflection of UEL, the current charge was lower than expected. In aggregate the charge is materially accurate. Overall we have concluded the Authority has made a slightly optimistic estimate, that is well within an acceptable range, and that the judgements surrounding infrastructure assets represent a valid assessment of asset usage.
Note 13: PPE: asset lives	3	3	N/A	We have reviewed management's assessment of property valuations and impairment calculations; confirmed the information provided to the valuer from the Authority; and compared the assumptions made by your valuer to benchmarks and to the assumptions used for 2016/17 for consistency. Overall we have concluded the Authority has made a balanced estimate and that the judgements represent a valid assessment of asset usage.
Note 24: Pension liability (Pension Reserve)	3	3	£685M (PY:£715M)	The Authority continues to use Hymans Robertson in the Local Government Pension Scheme. Due to the overall value of the pension assets and liabilities, small movements in the assumptions can have a significant impact on the overall valuation. The individual assumptions adopted by the actuary compared with our expected benchmark ranges are as set our below: • N/A Discount Rate: 2.7%. This is out with the benchmark range. • 1 Pension increase rate: 2.4%. This is deemed a cautious assessment, within the acceptable range. • 1 Life expectancy. This is deemed a cautious assessment, within the acceptable range. • 3 Salaries assumed to increase at 1.1% above CPI, within the acceptable range. Not withstanding that the discount rate was outside our benchmark range, when the assumptions are considered together the overall position is within our benchmark range. In this regard the overall set of assumptions proposed by the Employer can be considered to be balanced relative to our central rates for a typical UK scheme with a weighted average duration of 17.7 years.

Financial statements audit

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Note 1: Accounting policies	3	3	n/a	We have reviewed the Authority’s accounting policies contained in the financial statements to ensure consistency with the relevant accounting standards and the CIPFA Code. We have also analysed any changes in accounting policy from the previous period. We have determined that the Authority's accounting policies are consistent with those set out in the CIPFA Code, with prior year accounting policies, and are consistent with our understanding of the Authority’s application of them.
Note 4: Earmarked Reserves	3	3	£125M (PY:£138M)	We have reviewed the Earmarked Reserves disclosure for reasonableness and agreed all significant movements between reserves to confirm they are appropriate and have been authorised by the relevant individual. In addition to the earmarked reserves noted, the Council continues to work with £15M of working general fund balance. We believe the Authority’s judgement to be balanced.

Financial statements audit

Narrative report and Annual Governance Statement of the Authority

We have reviewed the Authority's narrative report and Annual Governance Statement and have confirmed that it is consistent with the financial statements, guidance and our understanding of the Authority.

Pension fund audit

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

Pension fund annual report

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

Queries from local electors

We did not receive any questions or objections from members of the public this year, but have one outstanding query from 2016/17.

Section Two

Financial statements audit

Audit opinion

We anticipate completing our responsibilities in relation to the audit of the accounts for the year end 31 March 2018 and anticipate issuing our audit opinion by the 31 July 2018.

Whole of Government Accounts (WGA)

We received your WGA consolidation pack and work is ongoing in relation to this. We anticipate issuing an unqualified consistency report.

Other grants and claims work

We undertake other grants and claims work for the Authority that does not fall under the PSAA arrangements. The status of our grants and claim work is presented below:

- Teachers Pensions: The reporting accountant assurance deadline is the 30 November 2018. We will complete the fieldwork in relation to this in October 2018; and
- Pooling of Housing Receipts: The reporting accountant assurance deadline is the 30 November 2018. We will complete the fieldwork in relation to this in October 2018.
- Education and Skills Funding Agency Subcontractor Grant Claim: The reporting accountant assurance deadline is the 14 September 2018. We will complete the fieldwork in relation to this in October 2018.
- Our work on the certification of Housing Benefits (BEN01) is planned for August 2018.

The fees charges in relation to this work are set out in Appendix 4.

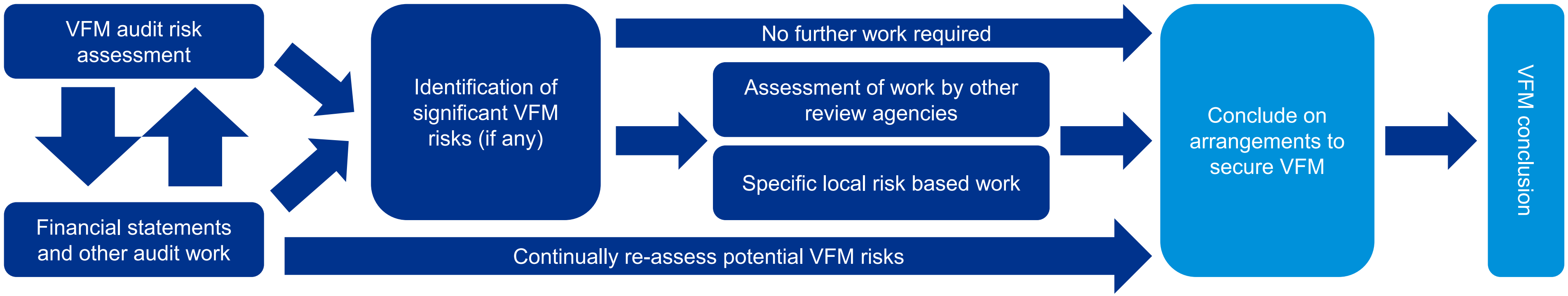
Section Three

Value for money

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

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

We follow a risk based approach to target audit effort on the areas of greatest audit risk as summarised below:



We did not identify any significant VFM risks and provide a summary below of the other areas of audit focus arising from our VFM work. We are satisfied that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2018, based upon the criteria of informed decision making, sustainable resource deployment and working with partners and third parties.

Value for money

VFM audit work

As reported within our Audit Plan, we did not identify any significant risks for the VfM conclusion. However we identified two areas of audit focus. Our findings in relation to these are outlined below.

VFM area of focus	Why this risk is significant	Our audit response and findings
Medium Term Financial Planning	**Risk:** In 2017/18 the Council had budgeted general fund expenditure of c.£1 billion services including: Adult Social Care, Children's Services, Housing, Environmental Services, Libraries and Public Health.	We have reviewed the controls the Authority has in place to ensure financial resilience, including how the Authority identifies, approves, and monitors savings plans and how budgets are managed throughout the year. We have also reviewed the Medium Term Financial Plan (2017/18 – 2019/20) to ensure that it has taken into consideration factors such as funding reductions, salary and general inflation, demand pressures, restructuring costs and sensitivity analysis given the degree of variability in the above factors. 2017/18 has been a challenging year for the Authority. Significant areas of financial pressure have included Childrens, Adult Social Care and Community Health (CACH) with a budget overspend of £3.3M. Overall, the Authority out turned revenue underspend of £0.046 million. There is ongoing pressures CACH, which whilst not unique to Hackney represents a significant financial risk going forward, in addition to pressures around the Dedicated Schools Grant. The position is strictly monitored and reported regularly to those charge with governance for further oversight and scrutiny. General Fund earmarked reserves have reduced from £138M to £125M together with an additional £15M of working balances. The Council held c£109.6M of cash and short term investments at the start of the year. This stood at £126.3M at the 31 March 2018. No new long term borrowing was taken in 2017/18. Total capital spend for 2017/18 was £271M, £8M below the final approved budget. Slippage on the capital budget has been closely monitored with elements carried forward to 2018/19 where appropriate. Risk management controls are in place to manage large scale and complex schemes. The 2018/19 budget is more challenging. The budget was approved in February 2018 and included significant savings together with the decision to increase Council tax by 3% to help fund social care, looked after children, day care and the cost of housing those in need. Alongside this, the Council continue their ambitious capital plan, investing £500 million including the building of 3,000 new homes

Value for money

VFM area of focus	Why this risk is significant	Our audit response and findings
Contract Monitoring and Managed Services	**Risk:** The Authority continues to work closely with partners and third parties, either through joint agreements or the more standard commercial contract with the third party providing the service. Having gone through competitive tendering processes in line with the Authority's regulations, it is vital that contract terms and agreed performance indicators are monitored closely to ensure that the Authority obtains maximum value for money from these contracts.	We have selected two contracts, including the Section 75 integrated social care contract, to review and to obtain an understanding of the controls that are in place to monitor the contract, both from a financial viewpoint but also that the quality of the service provided meets the contract specification. Aligned to this we have reviewed the Authorities risk management processes to ensure that risks arising from such projects are captured, recorded, reported and mitigating actions implemented where necessary. Whilst work is ongoing in this area, we would note that the Authority has continued to focus increased resources to refine contract management services.

Appendix 1

Recommendations raised and followed up

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

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

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
1	❷	**Payment of untaken annual leave upon contract termination** We noted that untaken annual leave had frequently been paid out to employees whom had accumulated annual leave at the time of termination. This is inconsistent with the Hackney redundancy policy which indicates that "Annual leave should normally be taken before the last day of service and only in exceptional circumstances will untaken annual leave be paid". We would recommend that this policy revisited to ensure that policy and process are aligned.	Agree to review the corporate redundancy policy compared to process and practice. The best and most appropriate way of aligning the policy and practice will then be considered and implemented. Officer: Dan Paul Due Date: End of December 2018
2	❷	**Pension Fund: Processing of leavers** Within our sample testing we identified instances where officers have left the authority, have ceased receiving payment, but have not had their status updated within the pension fund. This appears to be due to notification of the status change, not having been passed to Equiniti – the pension fund administrator. The Authority should identify and work to ensure accurate records are held of pensionable status, both locally and within the pension fund.	Agree for review of process and practice in this area, across LBH and Equiniti, to improve integrity and accuracy. Officer: Michael Honeysett Due Date: End of December 2018

There were no recommendations raised as a result of our work in 2016/17 for follow up.

Materiality and reporting of audit differences

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

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

We used the same planning materiality reported in our External Audit Plan 2017/18.

Materiality for the Authority's accounts was set at £15 million which equates to around 1.3% of gross expenditure.

Materiality for the Pension Fund was set at £23 million which equates to around 1.6% of net assets.

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

Reporting to Audit Committee

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

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £750k for both the Authority and for the Pension Fund.

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

Appendix 3

Audit differences

Unadjusted audit differences

Under UK auditing standards (ISA (UK&I) 260) we are required to provide the Audit Committee with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements.

Note 13: PPE – Revaluation increase

At the year end, an estimated indexation % was applied to PPE assets as actual indices were not available until July 2018. Review of the actual v's estimated indices in July 2018 identified a difference of £20.6m across all assets held by the Council. £18.5m of the variance related to HRA assets and has been adjusted. The remainder, £2.2m remain unadjusted.

Pension Fund

There are no uncorrected audit differences to the pension fund as at the date of this report.

Adjusted audit differences

Note 13: PPE – Revaluation increase

As noted above at the year end, an estimated indexation % was applied to PPE assets as actual indices were not available until July 2018. Review of the actual v's estimated indices in July 2018 identified a difference of £20.6m (uplift) across all assets held by the Council. £18.5m of the variance related to HRA assets and has been adjusted. The remainder, £2.2m remains unadjusted.

Note 44: Return on Assets (Pension Fund)

The IAS 19 report has been updated to reflect actual return on assets, replacing the previous estimate. This increases the return on assets figure from £7.5M to £24.9M.

Pension Fund

There are no presentational differences to the pension fund. There were however a number of casting and presentational errors within Note 44 (Defined Benefit Pension Schemes) within the main Authority accounts.

Appendix 3

Audit differences

Presentational Changes

A number of presentations adjustments were identified as noted below, together with a number casting errors, that have been corrected. The most significant of these related to the senior officers remuneration note where remuneration in relation election roles had been omitted from total remuneration. This has been amended in the final statements.

Additional narrative: CIES

An additional narrative has been included to the CIES to explain the reclassification of prior year balances.

Note 7, Note 28 and Long Term creditors:

Minor presentational adjustments for misclassifications.

Note 17: Financial Instruments - PFI liability

The Long term PFI liability for 1617 has been incorrectly rolled forward from the 1617 audited accounts, therefore it is in the draft accounts as £14,822K but it should be £14,112K.

Note 30: Agency Services

Minor narrative changes have been added to this note to reflect changes in the insurer details.

Note 32: Audit Fee

Updated to reflect the 4 grants which we will complete in the year, the total for which is £49,866.

Note 34: Exit Costs

Presentational changes to the content of this note include: Update to PILON amounts included in individual settlements, inclusion of annual leave and additional benefits as a termination benefit.

Note 41: Leases

We noted that for a lease agreement, there were separate land and building components. The land component had not been recognised as an operating lease nor has it been recognised as any other type of lease. This has been adjusted in the note.

Pension Fund:

Note: Management Expenses:

Audit Fees are noted as £18K. The correct figure is £21K (excluding VAT).

Audit independence

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF THE London Borough of Hackney

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

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

This Statement is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses: general procedures to safeguard independence and objectivity; breaches of applicable ethical standards; independence and objectivity considerations relating to the provision of non-audit services; and independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners, Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through: instilling professional values; communications; internal accountability; risk management; and independent reviews.

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

Appendix 4

Audit independence

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

Summary of fees

We have considered the fees charged by us to the authority and its controlled entities for professional services provided by us during the reporting period. Total fees charged by us for the period ended 31 March 2018 can be analysed as follows:

	2017-18 £	**2016-17 £**
Audit of the Authority	226,320	226,320
Audit of the Pension Fund	21,000	21,000
Total audit services	**247,320**	**247,320**
Allowable non-audit services	0	0
Audit related assurance services	11,250	11,250
Mandatory assurance services (Housing Benefits Grant Claim)	38,616	34,755
Total Non Audit Services	**49,866**	**49,866**

We are required by AGN 01 to limit the proportion of fees charged for non-audit services (excluding mandatory assurance services) to 70% of the total fee for all audit work carried out in respect of the Authority under the Code of Audit Practice for the year. The percentage of non-audit fees to audit fees for the year was 20%. We do not consider that the total of non-audit fees creates a self-interest threat since the absolute level of fees is not significant to our firm as a whole.

Appendix 4

Audit independence

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

Description of scope of services	Principal threats to independence and Safeguards applied	Basis of fee	Value of services delivered in the year ended 31 March 2018 £	Value of services committed but not yet delivered £
Audit-related assurance services				
Grant Certification – Teachers Pensions Return and Pooling of Housing Capital Receipts Return, Learning Skills grant	The nature of these audit-related services is to provide independent assurance on each of these returns. As such we do not consider them to create any independence threats.	Fixed Fee	11,250	11,250
Mandatory assurance services				
Grant Certification – Housing Benefit Subsidy Return	The nature of this mandatory assurance service is to provide independent assurance on each of the returns. As such we do not consider it to create any independence threats.	Fixed Fee	38,616	34,755

Contingent fees

We have not agreed any contingent fees with the Authority.

Independence and objectivity considerations relating to other matters

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

Confirmation of audit independence

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

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

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

KPMG LLP

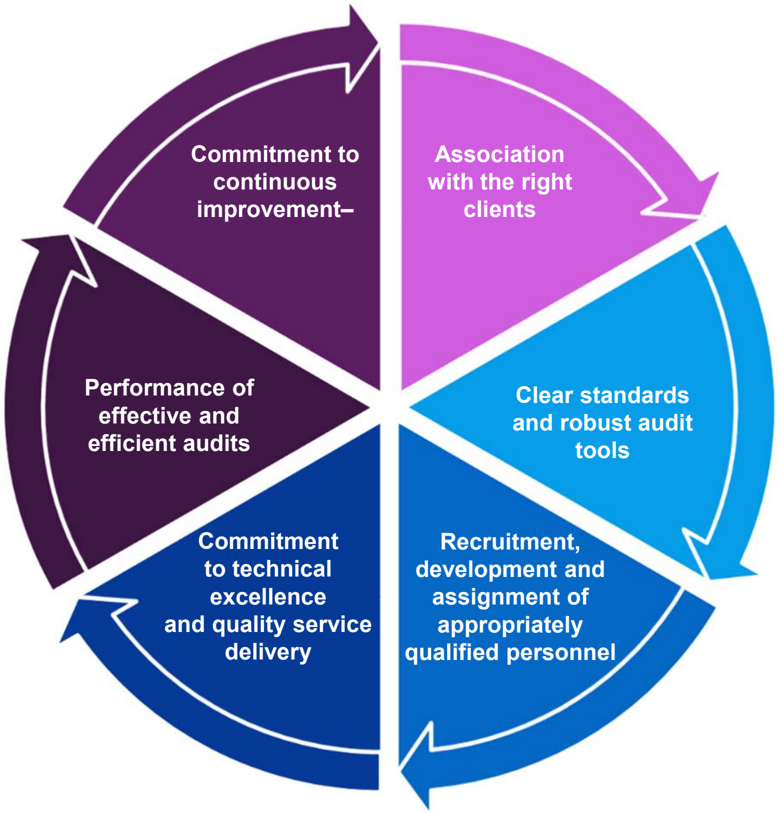
Appendix 5

Audit quality framework

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

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

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



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

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

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

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

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