Agenda Item No: 4

External Audit Report 2015/16

LGSS

January 2017

Contents

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Section one: Introduction

Introduction

This document summarises the key issues identified during our audit of the financial statements for the year ended 31 March 2016 for LGSS.

Scope of this report

This report summarises the key findings arising from our audit work at LGSS Joint Committee ('LGSS') in relation to LGSS's 2015/16 financial statements.

Financial statements

Our *External Audit Plan 2015/16*, presented to you in July 2016, set out the four stages of our financial statements audit process.

Planning → Control Evaluation → Substantive Procedures → Completion

This report focuses on the third stage of the process: substantive procedures. Our on site work for this took place during October and November 2016.

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

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 2015/16 financial statements of LGSS.

Our recommendations are included in Appendix one. We have also reviewed your progress in implementing prior year recommendations.

Acknowledgements

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

Section two: Headlines

Headlines

This table summarises the 2015/16 headline messages for LGSS. Section three of this report provide further details on each area.

Proposed audit opinion	We anticipate issuing an unqualified audit opinion on LGSS's 2015/16 financial statements subject to the following be completed: — audit review of the consolidation of LGSS Law Limited; — conclusion of the work in relation to the objection to the 2014/15 financial statements; and — receipt of a signed management representation letter. At that time we also expect to report that your Annual Governance Statement complies with guidance issued by CIPFA/SOLACE in June 2007.
Audit adjustments	Our audit has identified a total of 3 audit adjustments. The impact of these adjustments is to: — Decrease in both Gross Income and Gross Expenditure by £100k with no net impact on the deficit on provision of services; and — Decrease in both Assets and Liabilities of LGSS of £416k with no impact on the net worth of LGSS as at 31 March 2016. We have included further details of the adjustments in Appendix two. We anticipate that these will be corrected by LGSS. We have raised a number of recommendations to support management in improving this process in the future and reducing the number of adjustments, these are summarised in Appendix one.
Key financial statements audit risks	We identified the following risk to the financial statements in our 2015/16 External Audit Plan issued in July 2016: **Completeness of Income** This is the first year that LGSS has produced Group Accounts in order to consolidate its new subsidiary company, LGSS Law Limited. We have reviewed the plans in place to ensure complete and accurate accounting, including liaison with the subsidiary company in order to obtain sufficient and appropriate supporting information to support the process. We performed the audit of the subsidiary LGSS Law Limited and issued an unqualified audit opinion on 14 December 2016. At the time of this report we have not received the LGSS consolidation workings and therefore have not completed the audit of the consolidated numbers. We will provide a verbal update to the Committee on our work on the consolidation and if any issues have been identified. We worked with Officers throughout the year to discuss this key risk and our detailed findings are reported in section three of this report. There are no matters of any significance arising as a result of our audit work in this key risk area.

Headlines (cont.)

This table summarises the 2015/16 headline messages for LGSS. Sections three of this report provide further details.

Accounts production and audit process	We received a complete draft of the LGSS 2015/16 accounts by 30 June 2016. We agreed with management that the audit of LGSS should follow the completion of the audits of Northamptonshire and Cambridgeshire County Councils. We commenced the LGSS audit on 10 October 2016 and were provided with amended draft accounts and also the vast majority of working papers when we commenced our on-site visit. However, some working papers were not received for two to four weeks. Generally the working papers met the standards of our *Accounts Audit Protocol* however, there were notable exceptions in relation to debtors and creditors where the working papers did not reconcile to the financial statements. We found that officers generally responded to audit queries within one to weeks leading to some delays in the audit process. In some cases we did not receive evidence for four to five weeks after the request. This meant that we were unable to complete these areas of testing whilst we were still onsite, creating delays in the audit process. We have raised a recommendation for the improvement of the financial reporting process and also re-issued one of our prior year recommendations regarding Closedown team capacity. Details can be found in Appendix one. We have held a debrief with the Closedown Team on these matters, and will undertake a more detailed debrief with the Closedown team on conclusion of the audit. We would like to thank Officers for their assistance this year.
Completion	At the date of this report our audit of the LGSS 2015/16 financial statements is substantially complete subject to completion of our final review procedures, and resolution of outstanding queries including those in respect of consolidation of LGSS Law Limited and final review of the 2015/16 financial statements. We will provide a verbal update to the Committee on these areas. Before we can issue our 2015/16 opinion we require a signed management representation letter. 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 provide a draft of this representation letter to Director of Finance. We draw your attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are asking management to provide specific representations including those relating to pension liabilities. We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of LGSS's 2015/16 financial statements. The Committee should note that to issue our opinion on the 2015/16 financial statements will need to complete our work on the objection to the 2014/15 financial statements and as appropriate issue our opinion to those accounts.

Section three: Financial Statements

Proposed opinion and audit differences

Our 2015/16 audit has identified a total of two audit adjustments.

The impact of these adjustments has not yet been agreed as updated figures for cash, creditors and debtors are still to be provided by LGSS.

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

Proposed audit opinion

We anticipate issuing an unqualified audit opinion on LGSS's 2015/16 financial statements subject to the following be completed:

– audit review of the consolidation of LGSS Law Limited;

– conclusion of the work in relation to the objection to the 2014/15 financial statements; and

– receipt of a signed management representation letter.

Audit differences

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

The final materiality (see Appendix two for more information on materiality) level for this year's audit was set at £650,000. Audit differences below £32,000 are not considered significant.

Our audit identified a total of three significant audit differences, which we set out in Appendix two. Management have confirmed that these will be adjusted in the final version of the financial statements.

The table on the right illustrates the total impact of audit differences on LGSS's balance sheet as at 31 March 2016.

Balance sheet as at 31 March 2016		
£ 000	**Pre-audit**	**Post-audit**
Short term debtors	7,287	7,077
Cash and cash equivalents	0	0
Current Assets	**7,287**	**7,077**
Short term creditors	(4,584)	(4,168)
Provisions	(221)	(221)
Cash and cash equivalents	(456)	(661)
Current Liabilities	**(5,262)**	**(5,051)**

In addition, we identified a number of presentational adjustments required to ensure that the 2015/16 accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 ('the Code'). We understand that LGSS 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.

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

Significant audit risks

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

This section sets out our detailed findings on those risks.

In our *External Audit Plan 2015/16*, presented to you in July 2016, we identified the significant risks affecting LGSS's 2015/16 financial statements. We have now completed our testing of these areas and set out our evaluation following our substantive work.

The table below sets out our detailed findings for each of the risks that are specific to LGSS.

Completeness of Income

Risk description

LGSS is currently assessing whether they will be required to produce Group Accounts, in order to consolidate its new subsidiary company, LGSS Law Limited.

The Authority will need to ensure that they undertake a detailed and controlled review of the relationship that exists with LGSS Law Limited and assess whether consolidation is required, in order to ensure that the financial statements are prepared in accordance with the requirements of the CIPFA Code of Practice on Local Authority Accounting in the UK 2015/16 (the Code).

Findings

LGSS have assessed that they should produce Group Accounts to consolidate LGSS Law Limited. We have reviewed this against the Code and the *CIPFA Accounting for Collaboration* guidance and confirmed that LGSS Law Limited is not required to be consolidated.

Significant audit risks

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

This section sets out our detailed findings on those risks.

In our *External Audit Plan 2015/16* we reported that we would consider two risk areas that are specifically required by professional standards and report our findings to you. These risk areas were management override of controls and the fraud risk of revenue recognition.

The table below sets out the outcome of our audit procedures and assessment on these risk areas.

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Fraud risk of revenue recognition

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

In our External Audit Plan 2015/16 we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

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

Management override of controls

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

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

In line with our methodology, we carried out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.

Findings

As a result of LGSS using two ledgers we have taken a substantive approach to our audit testing. There are therefore no matters arising from this work that we need to bring to your attention.

Other areas of focus

In our External Audit Plan 2015/16, presented to you in July 2016, we identified two areas of audit focus.

These are not considered as significant risks but areas of importance where we would carry out some substantive audit procedures to ensure there is no risk of material misstatement.

We have now completed our testing. The table sets out our detailed findings for each of such areas of audit focus.

Non Pay Expenditure

We will undertake additional work on understanding the Accounts Payable system and the reports generated from this system. We will also complete testing over key system controls.

Findings

We have performed substantive testing over non pay expenditure as included in the Comprehensive Income and Expenditure Statement. This included testing reports generated from the accounts payable system for accuracy and completeness. Our testing did not identify any materials errors in the non pay expenditure balance. The processes to produce the balance from the host ledgers resulted in figures which were materially complete and accurate.

VAT Treatment

Following the objector challenge we consider VAT treatment by both host authorities to be a significant risk.

Findings

We have reviewed the management action taken to ensure VAT is treated consistently across both debtor balances. We have performed additional substantive testing over the treatment of VAT by both host authorities. Our testing did not identify any errors and VAT was treated consistently across both general ledgers.

Accounts production and audit process

Overall, working papers met the specified standard however were at times complex and a clear audit trail was not always evident.

Generally, Officers dealt with audit queries within one to two weeks of inquiry. However, there were instances where queries were not dealt with in a sufficiently prompt manner which has resulted in long delays of up to five weeks.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the significant qualitative aspects of LGSS's accounting practices and financial reporting. We also assessed LGSS's process for preparing the accounts and its support for an efficient audit.

Element	Commentary
Accounting practices and financial reporting	We consider that accounting practices are appropriate and incorporate those of LGSS Law Limited where applicable.
Completeness of draft accounts	The draft accounts were provided by 30 June 2016. We received revised accounts on 10 October 2016 when we commenced our on-site audit work. The vast majority of working papers were made available to us when we commenced our on-site audit work on 10 October 2016. Notable exceptions to this included an analysis of cash and cash equivalents, a CIPFA code checklist and an analytical review of the net cost of services. These items were not available for two to four weeks.
Response to audit queries	Officers generally dealt with audit queries within one to two weeks of inquiry, which resulted in significant delays to the audit process. Evidence relating to some areas of sample testing took four to five weeks to be provided, such as Income, Creditors and Non Pay Expenditure. Again such significant delays have had an impact on our audit.
Quality of supporting working papers	Our *Accounts Audit Protocol*, which we issued in August 2016 and discussed with Group Accountant – Closedown, set out our working paper requirements for the audit. The quality of working papers provided was variable but overall met the standards specified in our *Accounts Audit Protocol*. As each balance required input from both host authorities, the supporting working papers were at times complex and a clear audit trail was not evident. There was also little evidence of management review of the working papers. Working papers relating to debtors and creditors initially provided did not tie into figures disclosed in the draft financial statements, these had be reissued by LGSS. An additional working paper was also required to reconcile the figures to the trial balance. These issues caused significant delays in the audit.
Group audit	We have issued an unqualified opinion on the LGSS Law Limited financial statements. At the date of this audit report we have not received the consolidation workings for the LGSS financial statements. We will provide a verbal update to the Committee

As a result of the above we have raised a recommendation in respect of LGSS's working papers which is included in Appendix one.

We are currently discussing with Officers the impact of the delays in working papers and queries responses have had on the additional audit time incurred.

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of LGSS's 2015/16 financial statements.

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

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 LGSS for the year ending 31 March 2016, we confirm that there were no relationships between KPMG LLP and LGSS, 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 requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix three 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 Section 151 Officer for presentation to the Joint Committee. We require a signed copy of your management representations before we issue our 2015/16 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.

Appendices

Key issues and recommendations

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

LGSS 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	❶	**LGSS Financial Systems** As LGSS is not a separate legal entity it has been set up as a cost centre on the general ledgers of Northamptonshire County Council and Cambridgeshire County Council respectively. As a result the accounts closedown process is time-consuming, more complicated and less efficient than equivalent processes for similar organisations. Which in turn meant we were unable to place reliance on controls due to the requirement to test controls across two ledgers, and instead had to undertake much more time consuming substantive testing. In addition, due to the complex methodology used in compiling the Financial Statements this has led to the audit identifying a number of adjustments to be made by management and additional external audit testing to be performed.	**Management response** LGSS recognises that its accounting structure has become increasingly complex as it has expanded in recent years. LGSS will review its accounting structure and will explore the feasibility of setting up its own standalone General Ledger, in order to separate out its transactions from those of the councils. The overarching aim of LGSS when producing accounts is to make them as easy to read and understandable to the reader as possible. LGSS is committed to delivering this, and will continue to utilise the interim audit in order to run through proposed methodology with the external auditors and to work towards implementing changes to make the audit process smoother. LGSS will also explore the possibility of other potential changes to systems/processes, such as reviewing the feasibility of setting up its own bank account.

Key issues and recommendations (cont.)

No.	Risk	Issue and recommendation	Management response/responsible officer/due date
1 (cont.)		**Recommendation** As LGSS continues to grow, bringing in Milton Keynes following the yearend, it is now time to critically consider the financial systems and processes used by LGSS and implement a structure and/or system and processes that are more appropriate to the nature and size of the organisation. This will help to improve the controls in operation, accuracy of data, efficiency of the closedown process and ultimately reduce costs to the organisation of time required to prepare the accounts.	**Responsible Officer** LGSS Director of Finance / LGSS Head of Integrated Financial Services / LGSS Head of Business Planning and Finance. **Due date** This will be a major undertaking, the review to be completed by June 2017 for implementation in 2017-18. The ERP Gold implementation needs to be completed first.
2	2	**Quality of Prepared by Client working papers and responses to audit queries** We have noted an improvement in the clarity of LGSS's workings with regard to consolidating the two ledgers into the LGSS Financial Statements. However, throughout the audit we identified a number of issues where working papers provided by LGSS could not be agreed to the Financial Statements and/or errors were identified. This created delays in the audit as we were unable to test balances as working papers were not sufficiently complete to enable robust audit testing to occur. Our requests for further audit evidence, such as invoices for sample testing, also had significant delays of up to 35 days from the date requested, causing further audit delays. **Recommendation** LGSS should review its closedown process for 2016/17 and carefully consider any stretch targets for completion of working papers. LGSS should review the capacity on the Closedown Team to meet such targets, taking into consideration the Finance Team's workload also.	**Management response** The preparation of the 2015-16 accounts has been the first year that LGSS has utilised an Integrated Closedown Team. This team has prepared the accounts for LGSS, NCC and CCC. Producing these accounts and managing the subsequent audits simultaneously across the organisations has been challenging. LGSS will undertake a full debrief following the conclusion of the 2015-16 audit, looking at lessons learned and continuing to implement improvements for the future. A restructure of the Finance directorate has just been completed. This has included further strengthening of the Closedown function, and due consideration has been given to ensure that the team is appropriately resourced. Consideration will be given to the scheduling of the accounts production process, and of the audit fieldwork, when compiling the 2016-17 Closedown timetable to ensure that adequate resources are available to fulfil the required tasks. **Responsible Officer** LGSS Head of Integrated Financial Services **Due date** Restructure completed December 2016. Other aspects to be completed prior to audit of 2016-17 Accounts.

Key issues and recommendations (cont.)

No.	Risk	Issue and recommendation	Management response/responsible officer/due date
3	2	**Compliance with the CIPFA code requirements** 2015/16 was the first year LGSS were not legally required to produce financial statements. However, LGSS decided that they would, in the interests of openness and good governance, continue to produce financial statements. In doing so they have elected to apply the CIPFA Code of Practice on Local Authority Accounting. However, in undertaking our audit we identified a number of instances where disclosures required under the Code had been omitted and therefore these were required to be corrected by management. **Recommendation** LGSS should ensure that it continues to comply with the accounting requirements of the Code and ensure that any changes to the requirements are reflected in future LGSS financial statements.	**Management response** LGSS will continue to use the CIPFA Code of Practice as the basis of preparation for its Statement of Accounts in order to allow comparability with the accounts of the County Councils, which are prepared on that basis. In preparing its accounts LGSS has sought to balance the requirements of the Code with the desire to make the accounts understandable to the reader. On occasions this has required judgements to be made on the way to present particular items. For example, as LGSS's operations are considered to be trading income/expenditure the Code requires that they be presented as Financing and Investment income/expenditure on the face of the Income and Expenditure Statement. This does not provide the reader of the accounts with a breakdown of these figures by Directorate heading, so this has been shown in an additional table within the accounts. As 2015-16 has been the first year that LGSS Law has been trading it has been the first year that group accounts have been prepared. Upon preparation of the draft accounts judgements were made regarding the disclosures that would be required in respect of the consolidated LGSS Law statements. Following discussion with the auditors during the course of the audit it was agreed that some additional disclosures would be required. These have been included in the final set of accounts. For example disclosures have been added in respect of the defined benefit pension scheme. For the preparation of the 2016-17 accounts Officers will discuss any potential changes in presentation with the auditors at an early stage in the preparation process, in order to minimise changes required during the audit. **Responsible Officer** LGSS Closedown Group Accountant **Due date** Prior to the production of the 2016-17 LGSS Statement of Accounts.

Key issues and recommendations (cont.)

No.	Risk	Issue and recommendation	Management response/responsible officer/due date
4	3	**Journal entries** Journals can be requested by anyone within the LGSS Finance team without any prior management authorisation. There are no limits on the value of the journals. An annual review is in place however, the individual performing the review posts journals themselves, indicating a lack of segregation of duties. They are also required to review journals posted by more senior staff members, which they may be less likely to question or challenge if they seem unusual. **Recommendation** LGSS should consider exploring available options to improve its journal controls, including how the system can be utilised to support improved: • segregation of duties regarding the authorising, posting, reviewing and reconciling of journal entries; • access rights controlling who is authorised to record and approve journal entries along with the posting and authorisation limit; and • oversight of the journal entry-posting process by members of management including post-entry review based on a defined risk based approach.	**Management response** Journals can only be posted by staff with the appropriate responsibilities and sufficient professional knowledge. These staff are predominantly within the Finance, Pensions and Transactions teams. This functionality is not generally given to staff in the wider organisation. A validation process is undertaken prior to each journal being loaded. This checks that the template has been completed correctly and that the required information has been provided. Whilst there is no explicit approval at the point of entry, there are procedures in place to identify miss-postings retrospectively. Budget managers review the transactions posted against their budget groups as part of the monthly budget monitoring process. Finance Business Partner teams also scrutinise transactions and balances as part of this process. LGSS is currently in the process of implementing the ERP Gold system. Consideration will be given to ensure that an appropriate journal entry process is instigated in the new system. **Responsible Officer** LGSS Director of Finance **Due date** April 2017.

Follow up of prior year recommendations

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

This appendix summarises the progress made to implement the recommendations identified in our ISA 260 Report 2014/15 and re-iterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	3
Implemented in year or superseded	1
Remain outstanding (re-iterated below)	2

No.	Risk	Issue and recommendation	Status
1	2	**Supporting Working Papers** This is the second year that LGSS financial statements were required to be produced. Whilst the majority of the working papers provided were of good quality, in a number of areas we did not receive the evidence requested as part of our Prepared by Client list at the start of our onsite audit. In particular, this relates to payroll information from Cambridgeshire County Council (week 2 of our audit), and working papers in regards to recharges and journals which were provided at the end of our official visit. Additionally, we note that whilst there has been some improvement in providing consistency between the two Authorities (NCC and CCC), a number of key working papers are still presented in different formats which results in additional queries and delays in selecting samples. **Recommendation** LGSS should instigate robust closedown procedures to ensure that all PBC requested working papers are provided at the start of the audit, are produced in a consistent manner for efficient auditing, and are of sufficiently high quality to reduce the number of subsequent queries arising.	**Partially Implemented** The majority of working papers requested in our *Accounts Audit Protocol* were provided to us at the start of our onsite audit. However, there were a numbers of items outstanding which had to be requested again during the audit. In addition a number of working papers provided did not reconcile to the draft statement of accounts; these had be reissued by LGSS. We have therefore re-raised this recommendation for 2015/16.

Follow up of prior year recommendations (cont.)

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

This appendix summarises the progress made to implement the recommendations identified in our ISA 260 Report 2014/15 and re-iterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	3
Implemented in year or superseded	1
Remain outstanding (re-iterated below)	2

No.	Risk	Issue and recommendation	Status
2	2	**Closedown Resourcing** As noted in this report, during our audit visit, LGSS was subject to a number of queries arising from the public right of inspection. During this period, the two key Officers with responsibility for supporting the audit, had to prioritise their time in dealing with these elector queries. As an unfortunate result of this, we suffered delays in the completion of our audit, as LGSS took longer to respond to queries due to the fact that no other individual was able to assist in the resolution of these queries. **Recommendation** LGSS should reflect on this experience, and review its closedown process to ensure it has sufficient capacity of both time and resource to meet multiple commitments, including mitigation for unforeseen events such as public inspection queries, or other possibilities such as sick leave, annual leave etc.	**Not Implemented** Throughout the audit we encountered significant delays in receiving requested information. Notable examples include income and expenditure invoice samples requested, which took four to five weeks to be provided in full. We also encountered delays in our testing of termination benefits, as the key member of HR staff was absent with no other member of staff to help. This caused a delay of more than two weeks. We have therefore re-raised this recommendation for 2015/16.

Audit differences

This appendix sets out the audit differences.

The 2015/16 financial statements have been amended for all of the errors identified through the audit process.

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

Uncorrected audit differences

We are pleased to report that there are no uncorrected audit differences.

Corrected audit differences

Material misstatements
No material audit differences were identified over the course of our audit work.

Non material audit differences
Our audit identified a number of non material errors in the 2015/16 financial statements. These have been discussed with management who have agreed to make this adjustments in the financial statements. We have raised a recommendation in Appendix one to support LGSS in reducing the number of adjustments in future financial reporting periods.

Impact					
No.	**Income**	**Expenditure**	**Assets**	**Liabilities**	**Basis of audit difference**
1	Dr Gross Income £100k	Cr Gross Expenditure £100k	Dr Cash £100k Cr Debtors £100k		Remove loan to LGSS Law incorrectly included in the LGSS financial statements.
2			Cr Cash £416k	Dr Creditors £416k	Adjustment for 2014/15 Equalisation payment.
3			Dr Cash £110k Cr Debtors £110k		Adjustment for 2015/16 Equalisation payment.
	Dr £100k	**Cr £100k**	**Cr £416k**	**Dr £416k**	**Total impact of adjustments**

A number of minor amendments focused on presentational improvements have also been made to the draft financial statements. The Finance Department are committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Materiality and reporting of audit differences

For 2015/16 our materiality is £650k for LGSS's accounts.

We have reported all audit differences over £32k for LGSS's accounts to the Joint Committee.

Materiality

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

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

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

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

We used the same planning materiality reported in our External Audit Plan 2015/16, presented to you in July, 2016.

Materiality for LGSS's accounts was set at £650k which equates to around one percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the joint 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 Joint 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 LGSS, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £32k for LGSS.

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

Declaration of independence and objectivity

Communicate all significant facts and matters that bear on KPMG LLP's independence and objectivity and to inform you of the requirements of ISA 260 (UK and Ireland) Communication of Audit Matters to Those Charged with Governance.

Integrity, objectivity and independence

Professional ethical standards require us to communicate to you 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 judgment, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of Andrew Cardoza 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.

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 LGSS for the financial year ending 31 March 2016, we confirm that there were no relationships between KPMG LLP, LGSS, 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 requirements in relation to independence and objectivity.

Audit Fee

Our audit fee for 2015/16 was £24,500 plus VAT (£22,900 in 2014/2015, in addition to £33,000 fees billed to date with regards to work undertaken in order to respond to the objection raised in 2014/15).

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