KPMG

External Audit ISA260 Report 2017/18

Lincolnshire County Council and Lincolnshire Pension Fund

—

July 2018

Summary for Audit Committee

This document summarises the key findings in relation to our 2017-18 external audit at Lincolnshire County Council ('the Authority') and Lincolnshire Pension Fund.

This report covers our on-site work which was completed in June and July 2018 on the Authority's significant risk areas, as well as other areas of your financial statements, and the control environment in place to support the production of timely and accurate financial statements.

Financial statements

Subject to completion of the remaining work and all outstanding queries being resolved to our satisfaction we anticipate issuing an unqualified audit opinion on the Authority's financial statements before the deadline of 31 July 2018.

The remaining audit work includes the following matters:

- Final audit Director review;
- Addressing any remaining audit queries and any further matters arising from our completion procedures;
- General audit file completion and review procedures;
- Post balance sheet events review up to the date of signing the audit opinion; and
- Final review of the working papers and amended accounts.

Based upon our initial assessment of risks to the financial statements (as reported to you in our *External Audit Plan 2017/18* and updated during our audit) we identified the following significant risks (excluding those mandated by International Standards on Auditing) relating to the Authority:

— **Valuation of PPE** – the Authority operates a cyclical revaluation approach and we considered the way in which the Authority ensures that assets not subject to in-year revaluation are not materially misstated;

— **Pensions Liabilities** – we reviewed the processes in place to ensure accuracy of data provided to the Actuary and considered the assumptions used by the Actuary in determining the valuation.;

— **Faster Close -** the timetable for the production of the financial statements has been significantly advanced and we worked with the Authority in advance of our audit to understand the steps being taken to meet these deadlines and the impact on our work.

— **Agresso Upgrade** – the Authority has carried out a significant upgrade to Agresso during 2017/18 and we considered the Authority's arrangements for ensuring this upgrade process was managed effectively

There are two non material unadjusted audit differences arising from our work that we need to report to you (Appendix 3).

Based on our work, we have raised 1 recommendation. Details of our recommendation can be found in Appendix 1.

Control Environment

We have determined the overall control environment is adequate. We have included our findings at Section 1 of this report.

Summary for Audit Committee (cont.)

Accounts Production	The Authority's overall process for the preparation of the financial statements is effective. We have though identified continuing areas for improvement in the quality of the Authority's working papers for specific areas of the accounts, We have included our findings at Section 1 of this report.

Pension Fund financial statements

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

Based upon our initial assessment of risks to the Pension Fund financial statements (as reporting to you in our *External Audit Plan 2017/18* and updated during our interim visit) we have identified the following significant risks (excluding those mandated by International Standards on Auditing – see Page 9:

- **Faster close** – although the draft Pension Fund accounts have normally been available earlier than the Authority's statements the 31 May deadline was still expected to be challenging. As with the Authority's statements we worked with managers in advance of our audit to understand the steps being taken to meet these deadlines and the impact on our work Pension Fund audit work.
- **Agresso Upgrade** – The risk identified for the Authority and our response also applied to the Pension Fund audit.
- **Valuation of hard to price investments** – 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. We verified the existence of a selection of investments and considered the reliability of valuations reported by investment managers for harder to price investments.

There are no audit adjustments or audit differences arising from our work on the Pension Fund financial statements that we need to report to you.

Value for money arrangements

We have completed our risk-based work to consider whether in all significant respects the Authority has proper arrangements to ensure has taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We therefore anticipate issuing an unqualified value for money opinion

We set out our assessment of those areas requiring additional risk based work in our *External Audit Plan 2017/18* and have updated this assessment during our interim visit. As a result of this we have identified the following significant VFM audit risks:

- **Financial standing and medium term financial planning** – The Authority continues to face similar financial pressures and uncertainties to those experienced by others in the local government sector. The Authority needs to have effective arrangements in place for managing its annual budget, generating income and identifying and implementing any savings required to balance its medium term financial plan.
- **Corporate Support Services Provider's performance** – the Authority's management continues to work with the Corporate Support Services provider to strengthen the arrangements for managing the contract and ensure consistent performance to the expected standards across the full range of services provided.

See further details on page 22.

Summary for Audit Committee (cont.)

Whole of Government Accounts	The national audit deadline for reporting on authorities' 2017/18 Whole of Government Accounts (WGA) return is 31 August 2018. We have started the work required but it is unlikely that the information needed to complete the testing (including the 'matches' report from the Ministry of Housing Communities and Local Government) will be available in time to allow us to issue our report before 31 July 2018. We expect to complete the required audit work on the return in August 2018. We will update the Audit Committee if there are any significant audit matters arising from this work.
Exercising of audit powers	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.
Audit Certificate	The later deadline for the WGA audit work means that we expect to defer the issue of the Audit Certificate until that work is complete. There are no other audit matters at this stage that impact on the Audit Certificate.
Acknowledgements	We would like to take this opportunity to thank officers and Members for their continuing help

Section one

Control Environment

Organisational and IT control environment

We have identified no significant issues with the Authority's control environment and consider that the overall arrangements that have been put in place are adequate.

Organisational control environment

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit. We obtain an understanding of the Authority's overall control environment and determine if appropriate controls have been implemented. We do not complete detailed testing of these controls.

Controls over key financial systems

We have tested controls as part of our focus on significant audit risks and other parts of your key financial systems on which we rely as part of our audit. The strength of the financial system control framework informs the substantive testing we complete during our final accounts visit.

We have assessed the effectiveness of your key financial system controls, on which we rely as part of our audit. We found that the financial controls on which we planned to place reliance are operating effectively.

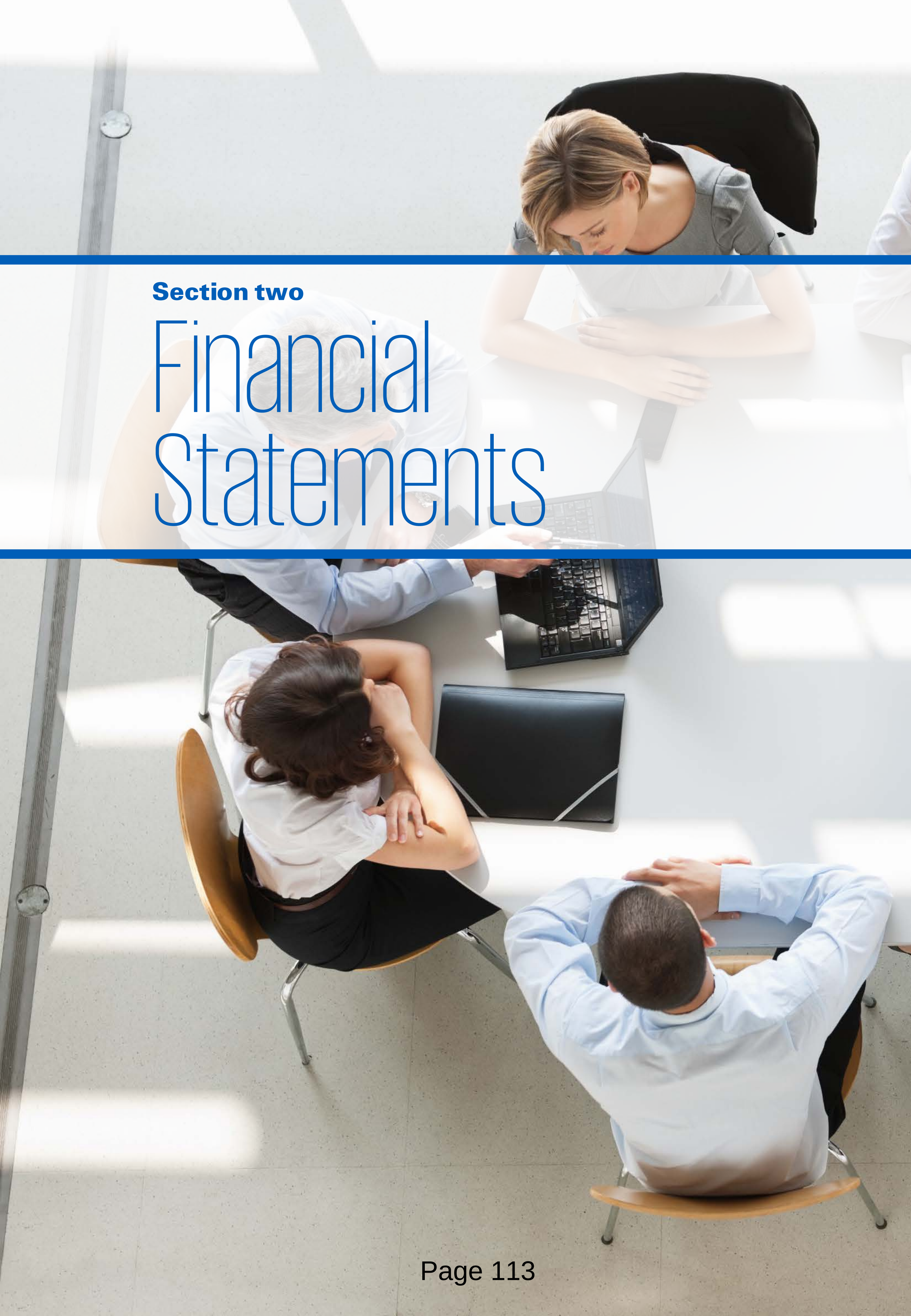
In our ISA 260 Report 2016-17 we identified issues and made recommendations relating to:

- Agresso General IT controls; and
- Payroll controls.

We have considered these areas again this year and provided further comments on the control deficiencies below:

- **Agresso General IT Controls** - in 2016-17 we carried out a range of procedures to assess controls around Agresso in respect of access to programs and data and program change control. The Authority was unable to provide us with sufficient evidence to demonstrate that adequate controls were in place in these areas. In particular, we noted that governance processes and the definition of responsibilities between the Authority and their supplier had yet to fully mature as the operation of the system moved from implementation project to business as usual. We have included at Appendix 2 management's update on the areas we highlighted for improvement. Although progress has been made in some areas we were again not able to rely on these controls for the current year and carried out the planned alternative procedures.
- **Payroll Controls** – in 2016-17 we carried out a range of procedures to assess the controls at the payroll provider and within the finance team surrounding payroll. These controls were not found to be designed or operating effectively which was consistent with the matters reported by Internal Audit during the year. We planned not to test payroll controls for 2017-18 as they had not be designed and operating for the full financial year and again adopted a fully substantive approach to testing. It is understood that finance and payroll have now adopted several controls which are now part of 'normal business' which should make the payroll process more robust going forwards.

Further details on the Authority's progress on these recommendations is included in Appendix 2.



Section two

Financial Statements

Accounts production and audit process

Audit standards (ISA 260) require us to communicate our views on the significant qualitative aspects of the Authority's accounting practices and financial reporting.

We also assessed the Authority's process for preparing the accounts and its support for an efficient audit. The efficient production of the financial statements and good-quality working papers are critical to meeting the tighter deadlines.

The Authority's overall process for the preparation of the financial statements is effective.

The Authority has made progress in implementing the recommendations from our 2016-17 ISA Report but there are still some areas for improvement.

Accounts practices and production process

The Authority published a complete set of draft accounts by 31 May 2018. We consider that the overall process for the preparation of your financial statements is effective. We have though identified continuing areas for improvement in the quality of working papers, as set out below.

We also consider the Authority's accounting practices appropriate.

Going concern

The financial statements of both the Authority and the Pension Fund have been prepared on a going concern basis. We confirm that we have identified no significant matters which would, in our view, affect the ability of the Authority or Pension Fund to continue as a going concern.

Implementation of recommendations

We raised three recommendations in our ISA 260 Report 2016-17 relating to the Authority's financial statements audit. Further details on the Authority's progress on these recommendations is included in Appendix 2.

Completeness of draft accounts

The Authority published a complete set of draft accounts on 31 May 3018, which is the statutory deadline.

Quality of supporting working papers

Our Accounts Audit Protocol sets out our audit approach and timetable. It also summarises the working papers and other evidence we require the Authority to provide to support our audit work. This helps the Authority and the Pension Fund to provide audit evidence in line with our expectations. We followed this up with a meeting with Management to discuss specific requirements of the document request list.

We found issues in relation to certain working papers for the Authority's financial statements, with the quality of audit evidence initially provided not meeting the requirements set out in our Accounts Audit Protocol 2017-18. This lead to delays in completing our work and placed additional pressures on the audit. The quality of audit papers has been reiterated as a continuing recommendation in Appendix 2.

Response to audit queries

The weaknesses in working papers and other matters identified during the audit resulted in a relatively high number of queries needing to be raised with officers. We appreciated the hard work carried out by our lead contact in processing this heavy workload, in keeping us informed on progress and trying to keep the delayed responses to a minimum. Inevitably some our queries took longer to fully resolve than others, particularly when responses or supporting evidence for our sample testing were required from officers outside of the core finance team. This delayed the audit process although we expect though to resolve any remaining queries by the date of giving the audit opinion.

Pension Fund audit

The audit of the Fund was completed alongside the main audit. There are no specific matters regarding the accounts production and audit process to bring to your attention relating to this.

Specific audit areas

We anticipate issuing an unqualified audit opinion on the Authority's 2017-18 financial statements and those of the Pension Fund by 31 July 2018.

Auditing standards require us to consider two standard risks for all organisations. We consider these as a matter of course in our audit and will have set out the findings arising from our work in our ISA 260 Report below.

Over the following pages we have set out our assessment of the specific significant risks and areas of audit focus we identified in relation to the audit of the Authority's financial statements and those of the Pension Fund.

01

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.

There are no matters arising from this work that we need to bring to your attention.

02

Fraudulent 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 2017-18* 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.

Specific audit areas

Significant Audit Risks – Authority

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

Risk:	**Valuation of PPE** 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 the required 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.
Our assessment and work undertaken:	We reviewed the approach that the Authority has adopted to assess the risk that assets not subject to valuation are materially misstated and considered the robustness of that approach. In relation to those assets which had been revalued during the year we assessed the valuer's qualifications, objectivity and independence to carry out such valuations and considered the methodology used. Subject to completion of any remaining work and any outstanding queries being resolved to our satisfaction we have determined that the assets which had not been revalued in year were not materially misstated. We have set out our view of the assumptions used in relation to accounting for Property, Plant & Equipment at page 15.

Specific audit areas (cont.)

Significant Audit Risks – Authority (cont.)

Risk:

Pension Liabilities

The net pension liability represents a material element of the Authority's balance sheet. The Authority is an admitted body of Lincolnshire 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.

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.

Our assessment and work undertaken:

As part of our work we reviewed the controls that the Authority has in place over the information sent to the Scheme Actuary. As part of this work we assessed the controls with respect to the management review of assumptions used in the valuation report and accounts.. We also evaluated the competency, objectivity and independence of the Fund's Actuary.

We reviewed the appropriateness of the key assumptions included within the valuation and compared them to expected ranges and involved a KPMG Actuary to provide a specialist assessment of those assumptions. We also reviewed the methodology applied in the valuation by the Scheme's Actuary.

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.

Subject to completion of any remaining work and any outstanding queries being resolved to our satisfaction we have determined that the net pension liability had been properly accounted for and disclosed in the financial statements. We have set out our view of the assumptions used in valuing pension assets and liabilities at page 15.

Specific audit areas (cont.)

Significant Audit Risks – Authority (cont.)

Risk:

Faster Close

In prior years, the Authority has been required to prepare draft financial statements by 30 June and then final signed accounts by 30 September. For years ending on and after 31 March 2018 however, revised deadlines apply which require draft accounts by 31 May and final signed accounts by 31 July.

These changes represent a significant change to the timetable that the Authority has previously been required to work to. The time available to produce draft accounts has been reduced by one month and the overall time available for completion of both accounts production and audit is two months shorter than in prior years.

In order to meet the revised deadlines, the Authority may need to make greater use of accounting estimates. In doing so, consideration will need to be given to ensuring that these estimates remain valid at the point of finalising the financial statements. In addition, there are a number of logistical challenges that will need to be managed. These include:

- Ensuring that any third parties involved in the production of the accounts (including valuers and the Pension Actuary) are aware of the revised deadlines and have made arrangements to provide the output of their work in accordance with this;
- Revising the closedown and accounts production timetable in order to ensure that all working papers and other supporting documentation are available at the start of the audit process;
- Ensuring that the Audit Committee meeting schedules have been updated to permit signing in July; and
- Applying a shorter paper deadline to the July meeting of the Audit Committee meeting in order to accommodate the production of the final version of the accounts and our ISA 260 report.

In the event that the above areas are not effectively managed there is a significant risk that the audit will not be completed by the 31 July deadline.

There is also an increased likelihood that the Audit Certificate (which confirms that all audit work for the year has been completed) may be issued separately at a later date if work is still ongoing in relation to the Authority's Whole of Government Accounts return and the Pension Fund Annual Report. This is not a matter of concern and is not seen as a breach of deadlines.

Although the draft Pension Fund accounts have normally been available earlier than the Authority's statements the 31 May deadline will still be challenging. As with the Authority's statements we will work with managers in advance of our audit to understand the steps being taken to meet these deadlines and the impact on our work Pension Fund audit work.

Our assessment and work undertaken:

We liaised with officers in preparation for our audit in order to understand the steps that the Authority was taking in order to ensure it met the revised deadlines and the accounts and supporting working papers were of the required quality. We confirmed that there was no increased reliance on estimates as part of the closedown process. We confirmed that the Authority and the Pension Fund published a complete set of draft financial statements on 31 May 2018.

As a result of this work we determined that the earlier financial reporting requirement had been met.

Specific audit areas (cont.)

Significant Audit Risks – Authority (cont.)

Risk:	**Agresso upgrade** The Authority has made progress in addressing the difficulties experienced in operating Agresso following its implementation in 2015/16, although there are continuing issues relating to the processing and reconciliation of the Authority's payroll. The Authority is carrying out a significant upgrade to Agresso during 2017/18. This upgrade needs to be effectively managed to ensure the system operates properly and to minimise the impact on in-year processing and the year-end reporting. This risk applied to both the Authority and the Pension Fund.
Our assessment and work undertaken:	We considered the arrangements established to manage the upgrade, liaised with Internal Audit to take into account their findings and reports on the process, and discussed the progress made and outcome of the upgrade with management. The upgrade was completed ahead of the year end and the changes did not have a significant impact on the accounts production or our audit..

Specific audit areas (cont.)

Significant Audit Risks – Pension Fund

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

Risk:	**Valuation of hard to price investments** 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.
Our assessment and work undertaken:	As part of our audit of the Pension Fund, we independently verified a selection of investment existence and prices to third party confirmations. We also considered to what extent the Pension Fund management has challenged the valuations reported by investment managers for harder to price investments. As a result of this work we determined that these investments had been properly valued.

Specific audit areas (cont.)

Other areas of audit focus

In our *External Audit Plan 2017/18* we identified the following as those risks with less likelihood of giving rise to a material error but which are nevertheless worthy of audit understanding.

- **Schools cash balances** – the Authority's 2016/17 accounts included around £2.5m relating to the 2014-15 year-end balances for three prime account schools which have since converted to academy status. The relative amounts due to and from these schools were under dispute and there had been difficulties and delays in the Authority and the schools determining an agreed position. We have followed this up as part of our current year audit and confirmed that this issue has now been resolved.
- **Pension Fund investments fair value disclosures** – these disclosures are detailed and can involve difficult judgements to confirm the investments are correctly categorised and properly presented. We have audited the fair value disclosures as part of the Pension Fund audit and not identified an material misstatements

Other matters – Pension Fund

In addition to the risks set out above, if we receive specific requests from the auditors of other admitted bodies, we are required to support their audits under the protocols put in place by the PSAA for this purpose. We have completed the audit work requested by the other auditors and reported our findings to them.

Judgements

We have considered the level of prudence within key judgements in your 2017-18 financial statements and accounting estimates. We have set out our view below across the following range of judgements.

Level of prudence

0	1	2	3	4	5	6
Audit Difference	Cautious		Balanced		Optimistic	Audit Difference
	Acceptable Range					

Subjective area	2017-18	2016-17	Commentary
Property, Plant and Equipment (PPE) valuations	3	3	Valuations are consistent with information provided by the independent expert valuers. We have reviewed the arrangements and discussed the approach with managers. The Authority has not made any significant changes to its approach to asset lives or its valuation arrangements.
Valuation of pension assets and liabilities	3	3	There have been no significant changes in the approaches to determining the estimate. The Authority has again relied on an independent expert actuarial valuation for its estimates. We did not identify any concerns regarding the Authority's approach or the assumptions used. The reported balance, together with assumptions and disclosures for inflation, discount rate, salary growth, life expectancy etc. are consistent with the report from the external actuary.
Provisions	3	3	We have reviewed the Authority's approach to estimating its provisions and not identified any material misstatement or further issues of concern for the Authority's attention.
Investments	3	3	We have reviewed arrangements for determining the accurate values for the Authority and Fund's investments and financial instrument disclosures. We did not identify any concerns regarding the valuations recorded.
Disclosure of Retirement Benefit Plans (Pension Fund)	3	3	IAS 26 requires the present value of the Fund's promised retirement benefits to be disclosed (the liability is not included within the Net Assets Statement). There have been no significant changes in the approaches to determining the estimate. The Authority has again relied on an independent expert actuarial valuation for its estimates. We did not identify any concerns regarding the Authority's approach or the assumptions used.

Proposed opinion and audit differences

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority's 2017-18 financial statements following approval of the Statement of Accounts by the Audit Committee on 23 July 2018.

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 4]) for this year's audit was set at £12 million. Audit differences below £600k are not considered significant.

We did not identify any material misstatements. We identified two misstatements above our reporting threshold that have not been adjusted by management. We have provided more information on these items and the misstatements which have adjusted at Appendix 3. It is our understanding that these will be adjusted in the final version of the financial statements. None of the audit adjustments agreed during our audit impact on the Authority's movements on the General Fund or the year and balance sheet as at 31 March 2018.

We identified a small number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2017-18 ('the Code'). These presentational adjustments were not significant and there are none that we are required to bring to your attention in this report.

Annual governance statement

We have reviewed the Authority's final 2017-18 Annual Governance Statement and confirmed that it is not misleading and is consistent with other information we are aware of from our audit of the financial statements.

Narrative report

We have reviewed the Authority's 2017-18 narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Pension Fund financial statements

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing unqualified audit opinion on the Pension Fund's 2017-18 financial statements following approval of the Statement of Accounts by the Audit Committee on 23 July 2018.

Pension Fund audit

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

For the audit of the Fund we used a materiality level of £19 million. Audit differences below £900k are not considered significant.

There are no adjusted or unadjusted audit differences that we need to report to you.

Annual report

We have reviewed the Pension Fund Annual Report and confirmed that:

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

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

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's 2017/18 financial statements.

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

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Lincolnshire County Council and Lincolnshire Pension Fund for the year ending 31 March 2018, we confirm that there were no relationships between KPMG LLP and Lincolnshire County Council and Lincolnshire Pension Fund, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in [Appendix 5] 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 management for presentation to the Audit Committee. We require a signed copy of your management representations before we issue our audit opinion.

Other matters

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

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

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

Section three

Value for Money Arrangements

Specific value for money risk areas

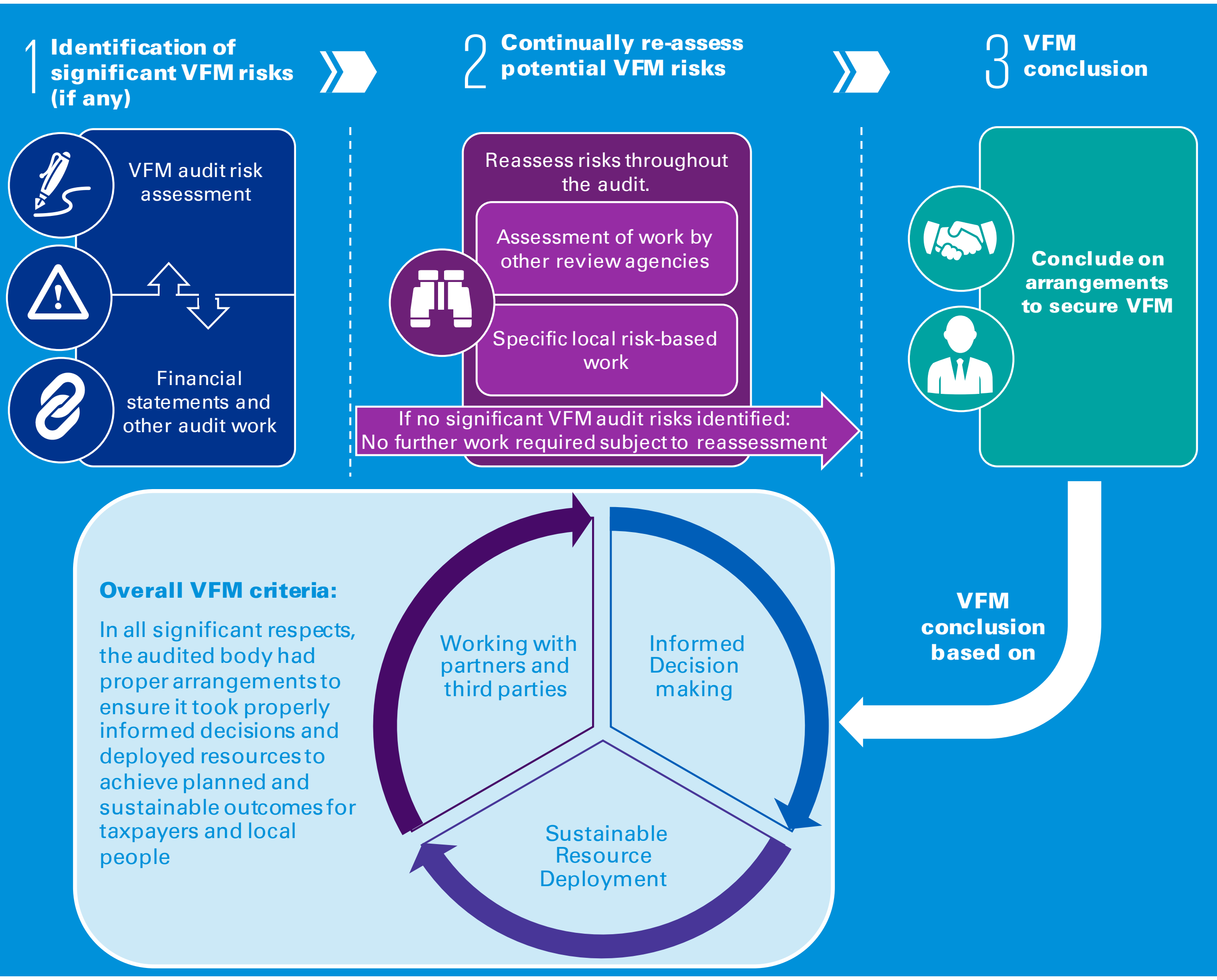
Our 2017-18 VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We have concluded that the Authority has made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

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.



Specific value for money risk areas (cont.)

The table below summarises our assessment of the individual VFM risks identified against the three sub-criteria. This directly feeds into the overall VFM criteria and our value for money opinion.

Applicability of VFM Risks to VFM sub-criteria

VFM Risk	Informed decision making	Sustainable resource deployment	Working with partner and third parties
Financial standing and medium term financial planning	✓	✓	✓
Corporate Support Services Provider's performance	✓	✓	✓

In consideration of the above, we have concluded that in 2017-18, the Authority has made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Further details on the work done and our assessment are provided on the following pages.

Specific value for money risk areas (cont.)

As communicated to you in our *External Audit Plan 2017-18*, and as updated throughout the audit, we have identified two risks requiring specific audit attention and procedures to address the likelihood that proper arrangements are not in place to deliver value for money.

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

We have provided below a summary of the risk areas identified, our work undertaken and the conclusions reached.

Risk: ***Financial standing and medium term financial planning***

The Authority continues to face similar financial pressures and uncertainties to those experienced by others in the local government sector. The Authority needs to have effective arrangements in place for managing its annual budget, generating income and identifying and implementing any savings required to balance its medium term financial plan.

Our work undertaken and assessment

As part of our additional risk based work, we reviewed the arrangements the Authority has in place in these areas and for ensuring its continuing financial resilience. We have considered the Authority's arrangements for managing its annual revenue and capital budgets, the 2017/18 outturn and the medium term financial plan. The 2017/18 revenue budget (excluding schools was underspent by £27.7m. The Authority had forecast the underspend during the year with the largest variance being in capital charges (£8m) and other budgets. The capital charges underspend reflects the slippage in the capital programme in the year and the lower than budgeted borrowing requirement. The reasons for the slippage in the capital programme are included in the July 2018 outturn report to the Authority's Executive.

In February 2018, the Authority approved a balanced 2018-19 budget. The budget included the required S.151 Officer assurances relating to the robustness of the budget and the adequacy of the level of reserves, but acknowledged the continuing risks around the delivery and timing of savings initiatives and the need to address the budget shortfall in future years. The budget was based on a balanced two year financial plan (including 2019-20) for revenue and capital budgets, taking the Council to the end of the current four year funding deal agreed with Central Government. This is a step forward from recent previous years when, given the uncertainty over funding and spending requirements, the Authority only published a financial plan for the next financial year. The 2018-19 budget again reflects a mixed approach to addressing the cost pressures identified (£26.9m), the reduced level of central grant funding and the estimated impact of the Lincolnshire Council's Business Rates Pilot introduced for 2018-19 (an overall increase of £7.5m in the Council's resources was estimated). The Authority approved:

- a 4.95% increase in Council Tax (3.99% in previous year), including 2% for the 'social care precept';
- savings of £23.1m (£39.5m in previous year) in Commissioning Strategy and Other Budgets; and
- A total transfer from reserves of £2.5m, which was much lower than the previous year budgeted transfer of £17.9m from the earmarked Financial Volatility Reserve. The 2019-20 budget does though see an increased reliance on this reserve, with nearly £34m expected to be transferred in that year.

The budget also reflects a further £8m funding support for continuing service transformation through the Flexible Use of Capital Receipts Strategy. The budget setting was informed by an October 2017 risk assessment which took into account a full assessment of the financial risks facing the Council, and challenged the underlying estimates, assumptions and contingencies. The budget acknowledges the need for continuing close monitoring of of savings and the further strengthening of financial management arrangements. The risks highlighted in the budget are consistent with those faced by others in the sector, particularly in relation to the demands on adult care services, and the medium term outlook for remains challenging. We are satisfied though that there were adequate arrangements in place at 31 March 2018 and there are no significant matters relating to this risk area which prevent us from giving an unqualified VFM conclusion.

Specific value for money risk areas (cont.)

Risk: ***Corporate Support Services Provider's performance***

The Authority's management continues to work with the Corporate Support Services provider and there is a significant level of resource aimed at strengthening the arrangements for managing the contract and ensuring consistent performance by the contractor to the expected standards across the full range of services provided. Given the general pressure on the Authority's resources it is important that the expected improvements in the contractor's performance are achieved and maintained

Our work undertaken and assessment

We considered:

- the key arrangements the Council had in place during 2017-18 and to date for managing this support services contract - there are wide-ranging formal arrangements in place and we confirmed they were in place.
- the Contractor's reported performance and the Authority's arrangements for scrutiny and challenge – the Authority has continued to apply and develop the framework, has regularly monitored performance and, if necessary, claimed service credits. The reported performance has improved during the year, particularly in the 2nd half with target service levels being achieved for virtually all services over that 6 month period.

The Authority has maintained its focus on the key areas of difficulty, most significantly relating to HR/Payroll and IT services, and has worked with the provider to try and address matters of continuing concern. Although progress has been mixed and in some areas not at the pace the Authority expected we are satisfied that overall there were adequate arrangements in place at 31 March 2018 and there are no significant matters relating to this risk area which prevent us from giving an unqualified VFM conclusion. We are aware that in May 2018 the Authority's Executive considered a report on the current support services contract, which is due to expire at the end of March 2020. The Executive approved a series of recommendations relating to the re-provision of the services included with the current contract by alternative providers. The Authority is currently engaging with the market and likely alternative provider organisations.

Appendices

Key issues and recommendations

We have set out in this appendix the recommendations arising from our audit work on the Authority's 2017-18 financial statements, together with management's responses. The Authority should closely monitor progress in addressing the risks, including the implementation of our recommendations.

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

Priority Rating for Recommendations

1	**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. Recommendations Raised: 0	2	**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. Recommendations Raised: 1	3	**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. Recommendations Raised: 0

Risk	Issue & Recommendation	Management Response
1	**Related Parties** ***Risk*** In the course of our work we tested the completeness and accuracy of the disclosures relating to councillors by cross checking their year end declarations to the Register of Interests and other information, including Companies House records. We identified some inconsistencies relating to one Councillor's return included in our sample. These findings have been shared with officers for follow up and we are satisfied the specific matters identified do not materially affect the accounts. ***Recommendation*** Managers should ensure there are robust arrangements for ensuring the Councillors' related party disclosures and other records (such as the Register of Interests) are complete and accurate.	The Finance Team has shared the auditor's findings with Committee/Member Services and the Council will look to improve the arrangements in preparation for the 2018/19 year end process. ***Responsible Officer*** Technical and Development Finance Manager ***Implementation Deadline*** For 2018/19 financial statements.

Appendix 2:

Follow-up of prior year recommendations

The Authority has made progress in relation to the recommendations we raised in the ISA 260 2016/17 but there are some areas which need to be improved further.

This appendix summarises the progress made to implement the recommendations identified in our *ISA 260 Report 2016/17* and re-iterates any recommendations still outstanding.

Number of recommendations that were	
Included in the original report	7
Implemented in year or superseded	2

Risk	Issue & Recommendation	Management Response	Status as at July 2018
1	**Working Papers** Virtually all of the required working papers were available by the agreed date and met the expected quality standards. There were some specific weaknesses in the working papers to support the staff cost notes in the accounts. Changes were required to both the working papers and these notes during the audit. ***Recommendation*** We recommend that the Authority ensure there are effective quality assurance arrangements in place for the production of the 2017-18 supporting working papers.	The Finance team had already identified various issues relating to this and external audit's other observations. Early training of Finance team is already planned in order to highlight and address the issues we have encountered in 2016-17.One of the planned training sessions will address the issue relating to the working papers and preparation of notes. There are various points that a preparer has to be aware in order to satisfy the requirements of the auditors and this will be communicated to the team to improve further the quality of the notes. Included in the planned work within Finance, we are currently looking at the various payroll reports we have used to prepare the notes to the accounts to identify the required changes in order to produce the notes. We are also putting in place a more robust process in reviewing the work when producing these notes. Further audit requirements by the auditors from Serco will continue to be managed through their Business Relationship Manager as we have found this to be effective.	The quality of the working papers was not consistently good across all areas for 2017-2018 and we have provided specific feedback to officers where required. This is an area where the finance team should continue to improve its arrangements. Management has provided the following response to this continuing recommendation: *The planned training of the Finance Team had taken place however following the audit, this identified further gaps and issues in our working papers. We will review the proformas we currently use and any changes will be communicated to the Finance Team through further training sessions.* *In order to ensure that the year-end timetable was met, various tasks had been allocated to those who were not previously involved in preparing working papers for audit. Whilst it helped us achieve the deadline, some of the working papers had fallen short on the expected quality. Therefore we will further strive to share best practices across the whole of the Team in order that the quality is consistent in all areas.* ***Recommendation continuing***

Follow-up of prior year recommendations

Risk	Issue & Recommendation	Management Response	Status as at July.2018
2	**Production of 2017-18 draft accounts and external audit** The draft financial statements were prepared and published by 30 June 2017. The Authority is in a relatively good position to meet the 31 May 2018 deadline for the publication of the 2017-18 draft financial statements. Nevertheless it needs to continue to ensure its arrangements are effective. The audit opinion deadline has also been brought forward to 31 July 2018 meaning that there will be much less time for the accountancy team to respond to and process any audit queries or changes to the draft financial statements. There was a relatively small number of audit queries this year and presentational errors in the 2016-17 draft financial statements identified during our audit, and these are to be corrected by management ***Recommendation*** The accountancy team should critically review its closedown arrangements and the format and likely content of the Statement of Accounts before the 2017/18 year-end and discuss its proposals with KPMG before the statements are produced.	We are now working on the closedown timetable in order to meet the early deadline. Early training of the Finance team to highlight and address the issues we have encountered in 2016-17 is already planned. Additionally, training is also being planned for budget holders to engage them and be aware of their role in the closedown process.	The draft accounts were prepared and published by the deadline. ***Recommendation implemented***
3	**School cash balances** Included within the total Cash and Cash Equivalents balance in hand is around £2.5m relating to the 2014-15 year-end balances for three prime account schools which have since converted to academy status. There are corresponding creditor balances in the accounts which off-set this balance. The relative amounts due to and from these schools are under dispute and there have been difficulties and delays in the Authority and the schools determining an agreed position. ***Recommendation*** We recommend the Authority progress this matter during 2017-18 and ahead of the year-end accounts.	The balance sheet review process will be strengthened this year. This will pick up any outstanding issues that will need resolving, like the School cash balances. We will continue to work with the auditors on any changes we will be making for the contents of the Statement of Account for 2017-18.	We have been informed by Irene Smith and our testing performed that this issue has been resolved and no longer appears as an issue in the 2017-2018 Statement of Accounts. ***Recommendation implemented***

Follow-up of prior year recommendations

Risk	Issue & Recommendation	Management Response	Status as at July.2018
4	**User Administration** We inspected documentation describing the existence of user administration processes; however the authority was unable to provide evidence to support the appropriateness of access provided to a sample of new starters. Furthermore, we identified a number of active user accounts associated with staff who had left the authority. Upon further investigation, it was established that there were weaknesses in the leavers' process due to reliance upon line manager notification and the absence of complimentary detective controls. ***Recommendation*** We recommend that the authority maintains a searchable record of user access requests in order to support accountability and provide an audit trail for statutory audit purposes. Furthermore, the authority should make improvements to the leavers' process to reduce reliance upon line manager notification as the primary control point and to eliminate the possibility of account re-use after an employee has left.	Agreed. From an IT perspective: The control of access to software systems and the management of Active Directory accounts is undertaken by the Council's IT Service Provider, Serco. There are technical controls which meet ISO27001 and PSN Co-Co obligations in place and Serco have processes and procedures to meet these obligations. All user access requests are managed via the IT Provider's IT Service Desk tool, Remedy On Demand (RoD) and therefore a log of all requests for audit purposes is available for audit purposes. At the point that the Serco IT Team are made aware of a Leaver, the process works well. However, the processes employed by the Serco HR Admin Team were historically poor and this has caused some issues.The data within Agresso, which should act as the trusted source for staff information is inaccurate and this has led to inaccuracies in the corresponding IT systems. A number of initiatives have been instigated to reduce this impact including a complete review of the starters, leavers and movers process across both HR and IT; unfortunately, these initiatives stalled. To mitigate these risks the Council has invested in Microsoft Identity Manager to streamline and workflow the changes in the HR system to system access, however this project is currently running in excess of two and a half years late due to delivery issues within Serco. From an Agresso System Administration perspective: The internal reporting for Agresso(LAGAN) requires further development to provide the information required for the Leavers process. This will be raised with the People Management Portfolio Board, however it is hoped that the current MIM project will address some of these weaknesses. However, the Council has a deliberate policy of not closing users on Agresso when people leave the Authority. This is because there may well be transactions in the system part-way through workflow, which need to be actioned by a nominated substitute. If the user record is closed, these transactions cannot be completed. Because access to the system is by single sign-on through the person's network logon, the risk of unauthorised access is very low, subject to the efficient working of the Leavers process (see comments and actions above).	The following update has been provided by management: *From an IT Perspective: Serco have recently re-started the Identity Management Project and a Project Manager and Technical resource has been assigned with build orders for the required servers in flight.* *Regarding the leaver process, an interim manual process to perform a rollup once a month upon leavers information from the Serco HR Function was agreed at the instruction of our Information Assurance Manager, David Ingham. This process is in place until a more automated process is enabled by delivery of the Identity Management Project.* *The current method of manually maintaining this process is still being completed by the Service Desk, and will continue until the Microsoft Identity Manager (MIM) is in place (the project is currently active). Cross checking will continue to validate AD accounts not active past 30 days once identified through HR leaver reports.* *From Agresso System Administration perspective: No changes have occurred. Liaison with LAGAN Administrators is expected to be an on-going liaison function.* Management's response confirms that the work to address the original recommendation is still in progress. ***Recommendation continuing***

Appendix 2:

Follow-up of prior year recommendations

Risk	Issue & Recommendation	Management Response	Status as at July.2018
5	**Change Management** We inspected documentation describing the existence of a change management process based upon ITIL principles; however, despite multiple requests to the authority and its supplier, we were not provided with any evidence to support the effective implementation or operation of this process. ***Recommendation*** The authority should maintain adequate records to demonstrate the effective operation of their change management processes in order to provide accountability for actions undertaken. This will support effective operational processes and the ability to roll-back in the event of a failed change, as well as providing an audit trail for statutory audit purposes.	Agreed. From an IT perspective: The IMT team manages the Change Advisory Board (CAB) process which protects the infrastructure and systems from ungoverned technical change; this is aligned with ITIL. Changes which are only impacting a single system is governed by the Governance Procedures within that user-group and would not be subject to CAB. From an Agresso System Administration perspective (for those changes which are not approved via CAB):This will be raised with the Agresso Governance Board (where all none CAB approvals are made), and more formal processes established for agreeing these changes.	The following update has been provided by management: *From an IT Perspective:* *ICT Quality Manager, David Rose – Allen has been working with the BW On Team to improve this process and can confirm that a satisfactory governance model is now being followed. It is not a mature model at this stage, but it is now widely accepted by the business and is an area that has been targeted for continual improvement. This will be continued to be reviewed and improved over the coming months.* *All changes, both technical and application level, are now presented to a governance board on a weekly basis. The board controls all change and acts a guardian to the system and its infrastructure. Application changes are reviewed and approved by this board whilst technical changes are reviewed and passed to formal CAB for approval.* *This board works in two capacities, one to approve change and one to manage the upcoming pipeline and control the business areas to ensure that they are planning and completing work as expected.* *From Agresso System Administration perspective: The BW governance Board process has been further strengthened, with revised processes and paperwork. Corporate IT involvement is also now increased, which ensures a strong link to data governance.* Management's response confirms that the work to address the original recommendation is still in progress. ***Recommendation continuing***

Appendix 2:

Follow-up of prior year recommendations

Risk	Issue & Recommendation	Management Response	Status as at July.2018
6	**Segregation of Duties** We established that there is no segregation of duties between development staff and those responsible for migration of changes into to the live environment. Whilst an informal system of management checks / peer review is used to check that actual changes to the live system has been carried out according to the approved configuration document, this check is not documented or evidenced. We were unable to establish any relevant monitoring or compensating controls to mitigate the associated risks and further noted that formal definition of appropriate access to change and development staff (including respective responsibilities of the authority and their supplier) is still under development. ***Recommendation*** We recommend that, where practical, access to undertake development and migrate changes to the live environment should be assigned to separate roles. Roles and responsibilities for the management of the live system, including the respective responsibilities between the authority and their supplier, should be agreed and documented.	Agreed. In terms of the comments on documentation this will be raised with the Agresso Governance Board, and more formal processes established for agreeing changes. Due to the size of the team it is feasible to have a division of duties between development of changes and application in the live environment. However, there is a process of peer review where work is developed and reviewed by different team members. There is also an established process of developing, building and testing before changes are migrated into the live environment to reduce the risk of manual error.	The following update has been provided by management: *The BW governance has been further strengthened. Otherwise there have been no changes made.* Management's response confirms that the work to address the original recommendation is still in progress. ***Recommendation continuing***

Follow-up of prior year recommendations

Risk	Issue & Recommendation	Management Response	Status as at July 2018
7	**Payroll Control Weaknesses** We have tested key opinion controls as part of our focus on significant audit risks and other parts of your key financial systems on which we rely as part of our audit. The strength of the control framework informs the substantive testing we complete during our final accounts visit. Payroll system controls continue to be a area of concern our audit approach to this was again largely substantive. There is overlap between these recommendations and the much broader set of recommendations raised in Internal Audit's reports to the Audit Committee. The areas of weakness identified during our testing included: • Payroll Exception Reporting –there have been no consistent and robust control throughout the year. The arrangements were unclear and the exception reports have been inconsistently run, saved and annotated. • Starters and leavers -from the testing carried out we identified a number of control deficiencies These included weaknesses in evidence to support authorisation of new starters or processing of leavers, and a number of employees' Agresso Accounts still being 'active' despite having left the organisation (a result of Payroll not properly terminating the employee on the Agresso System). The continuing weaknesses in the Payroll system controls are an area of concern and our audit approach to this was again largely substantive. ***Recommendation*** The authority should maintain adequate records to demonstrate the effective operation of their change management processes in order to provide accountability for actions undertaken. This will support effective operational processes and the ability to roll-back in the event of a failed change, as well as providing an audit trail for statutory audit purposes.	None requested	This has continued to be a concern in 2017-18 and highlighted again as a continuing recommendation. It is understood that finance and payroll have now adopted several controls which are now part of 'normal business' which should make the payroll process more robust going forwards. ***Recommendation Continued***

Audit differences

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit 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.

Adjusted Audit Differences – Authority and Pension Fund

There are no adjusted audit differences to the Authority or Pension Fund financial statements that we are required to report to you. During our audit a number of amendments were identified as required to the supporting notes to the Authority 2017-18 draft financial statements, to correct errors or to comply with the Code requirements. We understand the Finance team is to amend the statements for this matters and to update the Audit Committee on the changes made. We will review these amendments as part of our closing procedures and checks on the final set of the financial statements. The main audit differences related to notes 34 (Exit Packages) and note 35 (Termination Benefits) and these were amended to include £1.6m of redundancy expenditure which had omitted from the disclosure..

Unadjusted audit differences – Authority and Pension Fund

The following table sets out the uncorrected audit differences identified by our audit of the Authority financial statements for the year ended 31 March 2018. There are no unadjusted audit differences identified by our audit of the Pension Fund financial statements for the year ended 31 March 2018. These differences are individually below our materiality level of £12m. We have considered the impact of these unadjusted audit differences on the Authority's financial statements in forming our audit opinion.

Table 2: Unadjusted audit differences – Authority (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1	-	-	Cr Short Term Debtors £679k Dr Short Term Investments £679k	-	-	Acrrued interest of £679k on Short Term Investments has been included in Short Term Debtors, rather than with Short Term Investments.
2	Dr Expenditure (Cost of Services) £4,777	-	Dr PPE £2,063	Cr Accruals £6,840	-	Our testing identified a number of creditor transactions which had not, in error, been included in the year end accruals. This included one for £3,152k. The finance team further reviewed payments made in April and May 2018 to identify any additional payments made which related to 2017-18 and where an accrual had not been made. Further items over the year end de-minimis levels (revenue £25k, capital £50k) were identified, totalling £3,688k.
	Dr £4,777	**-**	**Dr £2,063**	**Cr £6,840**		**Total impact of adjustments**

Materiality and reporting of audit differences

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 2017-18*, presented to you in January 2018.

Materiality for the Authority's accounts was set at £12 million which equates to around 1.14 percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the 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, an individual difference is considered to be clearly trivial if it is less than £0.6 million for the Authority.

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

Materiality – Pension fund audit

The same principles apply in setting materiality for the Pension Fund audit. Materiality for the Pension Fund was set at £19 million which is approximately 0.88 percent of gross assets.

We design our procedures to detect errors at a lower level of precision, set at £0.9 million for 2017-18.

Required communications with the Audit Committee

We have provided below at-a-glance summary of the information we are required to report to you in writing by International Auditing Standards.

Required Communication	Commentary
Our draft management representation letter	We have not requested any specific representations in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2018.
Adjusted audit differences	We have identified no adjusted audit differences above out reporting threshold for the Authority and the Pension Fund financial statements. See Appendix 3 for further details.
Unadjusted audit differences	The net impact of the two unadjusted audit differences arising from the Authority audit would be to increase the deficit on provision of services by £4,777k. In line with ISA 450 we request that you adjust for these items. However, they will have no effect on the opinion in the auditor's report, individually or in aggregate. See Appendix 3 for further details. We have identified no unadjusted audit differences above out reporting threshold for the Pension Fund financial statements..
Related parties	There were no significant matters that arose during the audit in connection with the entity's related parties.
Other matters warranting attention by the Audit Committee	There were no matters to report arising from the audit that, in our professional judgment, are significant to the oversight of the financial reporting process.
Control deficiencies	We have set out our assessment of the Authority's internal control environment, including details of any significant deficiencies identified, in Section one of this report.
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts	We identified no actual or suspected fraud involving the Authority's Member or officers with significant roles in internal control, or where the fraud resulted in a material misstatement in the financial statements.
Significant difficulties	No significant difficulties were encountered during the audit.
Modifications to auditor's report	There are no modifications to our audit report.
Disagreements with management or scope limitations	The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit.

Required communications with the Audit Committee (cont.)

Required Communication	Commentary
Other information	No material inconsistencies were identified related to other information in the Narrative Report or Annual Governance Statement. These reports were found to be fair, balanced and comprehensive, and compliant with applicable requirements.
Our declaration of independence and any breaches of independence	No matters to report. The engagement team have complied with relevant ethical requirements regarding independence. See Appendix 6 for further details.
Accounting practices	Over the course of our audit, we have evaluated the appropriateness of the Authority's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate. We have set out our view of the assumptions used in valuing pension assets and liabilities at page 15.
Significant matters discussed or subject to correspondence with management	There were no significant matters arising from the audit which were discussed, or subject to correspondence, with management.

Declaration of independence

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF LINCOLNSHIRE COUNTY COUNCIL

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;
- 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
- Independent reviews.

The conclusion of the audit engagement leader as to our compliance with the FRC Ethical Standard in relation to the Lincolnshire Pension Fund audit engagement [and that the safeguards we have applied are appropriate and adequate] is subject to review by an engagement quality control reviewer, who is an Audit Director not otherwise involved in your affairs.

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

Declaration of independence (cont.)

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 for professional services provided by us during the reporting period. We have detailed the fees charged by us to the authority for significant professional services provided by us during the reporting period in Appendix 7, as well as the amounts of any future services which have been contracted or where a written proposal has been submitted. 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	107,325	111,101
Audit of the Pension Fund	24,350	25,344
Total audit services	**131,675**	**136,445**
Allowable non-audit services	Nil	50,000
Audit related assurance services	14,600	3,000
Mandatory assurance services	Nil	nil
Total Non Audit Services	**14,600**	**53,000**

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 relevant non-audit fees were 11.1% of the total fee for all audit work.. 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.

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 and controls report – Teachers Pensions Agency (TPA) Return, S31 Transport Grant and SFA Subcontracting return	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	TPA 5,500 S31 4,100 SFA 5,000	nil

Appendix 6:

Declaration of independence (cont.)

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 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 Audit Director 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.

John Cornett

Director, KPMG LLP

Appendix 7:

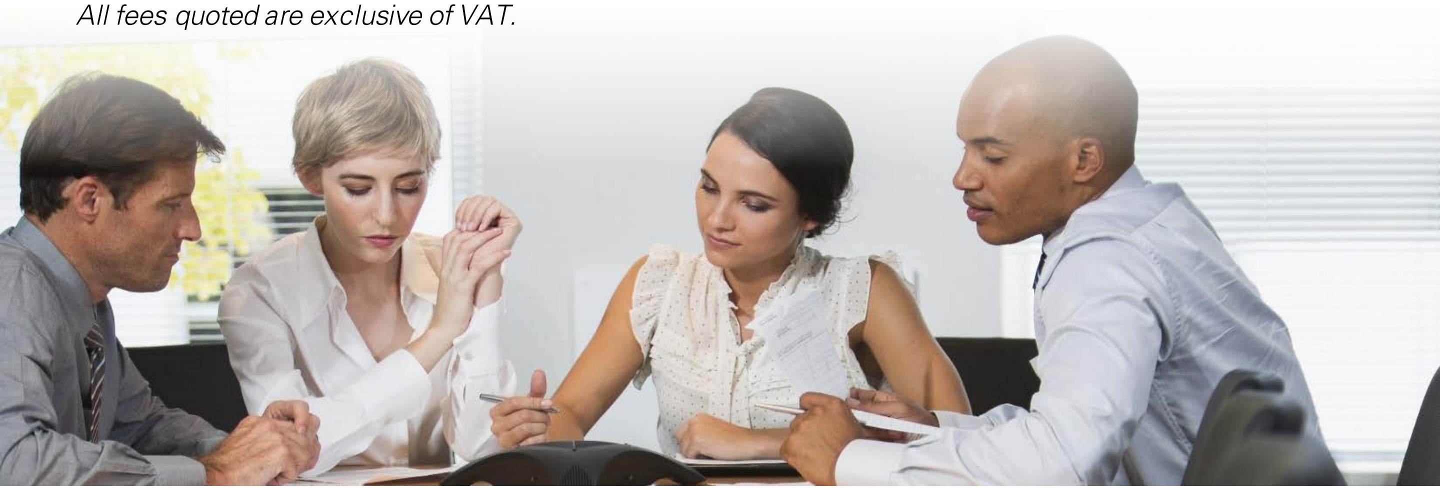
Audit fees

As communicated to you in our *External Audit Plan 2017-18*, our scale fee for the audit of the Authority is £107,325 plus VAT (£111,101 in 2016-17) and £24,350 plus VAT for the Pension Fund (£25,344 in 2016-17)

We propose an additional fee due to work undertaken in relation to the significant risk areas identified in this report, and to cover the costs of the KPMG experts and specialists we have needed to engage in response to matters identified during the audit. The amount of additional fee has still to be determined and is still subject to final agreement and PSAA approval. We will update the Audit Committee when this has been resolved.

Component of the audit	2017-18 Planned Fee £	2016-17 Actual Fee £
Accounts opinion and value for money work		
PSAA Scale fee Lincolnshire County Council	107,325	111,101
PSAA Scale fee Lincolnshire Pension Fund	24,350	25,344
Total audit services	**131,675**	**136,445**
Mandatory assurance services	Nil	Nil
Total mandatory assurance services	**Nil**	**Nil**
Audit-related assurance services		
Teachers' Pension Return 2016/17	5,500	3,000
S31Transport Grant 2016/17	4,100	Nil
SFA Subcontracts' Controls 2016/17	5,000	Nil
Total audit-related assurance services	**14,600**	**3,000**
Allowable non-audit services		
SERCO 'Lessons learned' review	**Nil**	**50,000**
Total allowable non-audit services	**Nil**	**50,000**
Total non-audit services	**-**	**53,000**
Grand total fees for the Authority	**146,275**	**189,445**

All fees quoted are exclusive of VAT.



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