Year End Report to the Audit & Risk Committee - DRAFT

London Borough of Lewisham

Year end report for the year ended 31 March 2024

—

12 December 2024

KPMG required communications for all entities

Important notice

This report is presented under the terms of our audit under Public Sector Audit Appointments (PSAA) contract.

The content of this report is based solely on the procedures necessary for our audit.

Purpose of this report

This Report has been prepared in connection with our audit of the consolidated financial statements of London Borough of Lewisham (the Authority), prepared in accordance with International Financial Reporting Standards (‘IFRSs’) as adapted Code of Practice on Local Authority Accounting in the United Kingdom 2023/24, as at and for the year ended 31 March 2024.

This Report has been prepared for the Authority's Audit and Risk Committee, a sub-group of those charged with governance, in order to communicate matters that are significant to the responsibility of those charged with oversight of the financial reporting process as required by ISAs (UK), and other matters coming to our attention during our audit work that we consider might be of interest, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone (beyond that which we may have as auditors) for this Report, or for the opinions we have formed in respect of this Report.

This report summarises the key issues identified during our audit.

Limitations on work performed

This Report is separate from our audit report and does not provide an additional opinion on the Authority’s financial statements, nor does it add to or extend or alter our duties and responsibilities as auditors.

Yours sincerely,

Fleur Nieboer
Partner KPMG LLP
12 December 2024

We have not designed or performed procedures outside those required of us as auditors for the purpose of identifying or communicating any of the matters covered by this Report.

The matters reported are based on the knowledge gained as a result of being your auditors. We have not verified the accuracy or completeness of any such information other than in connection with and to the extent required for the purposes of our audit.

Status of our audit

Our audit is not yet complete and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status. Page 3 ‘Our Audit Findings’ outlines the outstanding matters in relation to the audit. Our conclusions will be discussed with you before our audit report is signed.

Restrictions on distribution

The report is provided for the information of the Audit and Risk Committee of the Authority; that it will not be quoted or referred to, in whole or in part, without our prior written consent; and that we accept no responsibility to any third party in relation to it.

DRAFT

Our audit findings

Significant audit risks	Page 6-14
Significant audit risks	**Our findings**
Management override of controls	Our testing of journals which meet our high-risk criteria is substantially complete, with no findings to report.
Valuation of land and buildings	Our testing identified misstatements in relation to the presentation of Decent Homes expenditure, the valuation of Council Dwellings and the consideration of the Decent Homes standard being met, and movement in published indices after the Authority received the valuation report from the management expert. We also identified a control deficiency over management review of the PPE valuation assumptions and a presentational error in the property numbers disclosure. Our testing in this area is substantially complete.
Valuation of post-retirement benefit obligations	We involved KPMG actuarial specialists in reviewing the actuarial assumptions. Overall assumptions are assessed as balanced.
Key accounting estimates	**Page 21-22**
Valuation of council dwellings	We assessed as reasonable the assumptions underpinning the valuation. We have found the assumptions to be within our acceptable range.
Valuation of pension obligations	We assessed as reasonable the assumptions underpinning the valuation. We have found the assumptions to be balanced.

Uncorrected audit misstatements		Page 41
Understatement/ (overstatement)	**£m**	**%**
Revenues	0.0	0.0
Deficit for the year	0.0	0.0
Total assets	0.0	0.0
Total taxpayers' equity	0.0	0.0

Misstatements in respect of disclosures	Page 24
Misstatement in respect of Disclosures	**Our findings**
Property numbers	We identified a presentational error.

Number of control deficiencies	Page 44-51
Significant control deficiencies	0
Other control deficiencies	9
Prior year control deficiencies remediated	3

Outstanding matters

Our audit is substantially complete except for the following outstanding matters

- Finalisation of journals sample testing and post-close journals
- Queries on PPE valuation
- Queries on input data used in the valuation of defined benefit obligation.
- Final queries against non-significant business processes including business rates, bank reconciliations, receivables, staff costs controls
- One outstanding investment confirmation
- Rental income walkthrough
- Related parties testing
- Testing of non-material disclosures in the financial statements
- IFRS 16 pre-transition disclosures
- Going concern
- Subsequent events
- Management representation letter
- Draft annual report to KPMG
- Finalise audit report and sign

Key changes to our audit plan

We have not made any changes to our audit plan as communicated to you on 11 September 2024, other than as follows:

Other changes	Risk change	Effect on audit strategy and plan
Change in significant risk	Valuation of council dwellings	In our audit plan we stated that we had a significant risk over land and buildings. As a result of our risk assessment procedures, we have separately considered this risk over the different property types and valuation methodologies applied at the Authority. We have refined this significant risk to apply to council dwellings only, and the application of an appropriate methodology to the valuation.
Change to response to significant risk	Valuation of land and buildings	In our audit plan we stated that we expected to utilise KPMG valuation specialists to support in our work over the valuation of land and buildings. As a result of our risk assessment procedures we determined that full involvement of KPMG specialists was not required. KPMG specialists have provided sector insight to all local government audit teams.
Change to response to other audit risk	Risk of error from expenditure recognition	In our audit plan we described that we would perform a retrospective review of prior year accruals in order to assess the completeness with which accruals had been recorded at 31 March 2023 and consider the impact on our assessment of the accruals at 31 March 2024. We performed alternative risk assessment procedures including a year on year comparison of accruals and an assessment of whether accruals contain estimation uncertainty.

DRAFT

Significant risks and other audit risks

We discussed the significant risks which had the greatest impact on our audit with you when we were planning our audit.

Our risk assessment draws upon our knowledge of the business, the industry and the wider economic environment in which London Borough of Lewisham operates.

We also use our regular meetings with senior management to update our understanding and take input from local audit teams and internal audit reports.

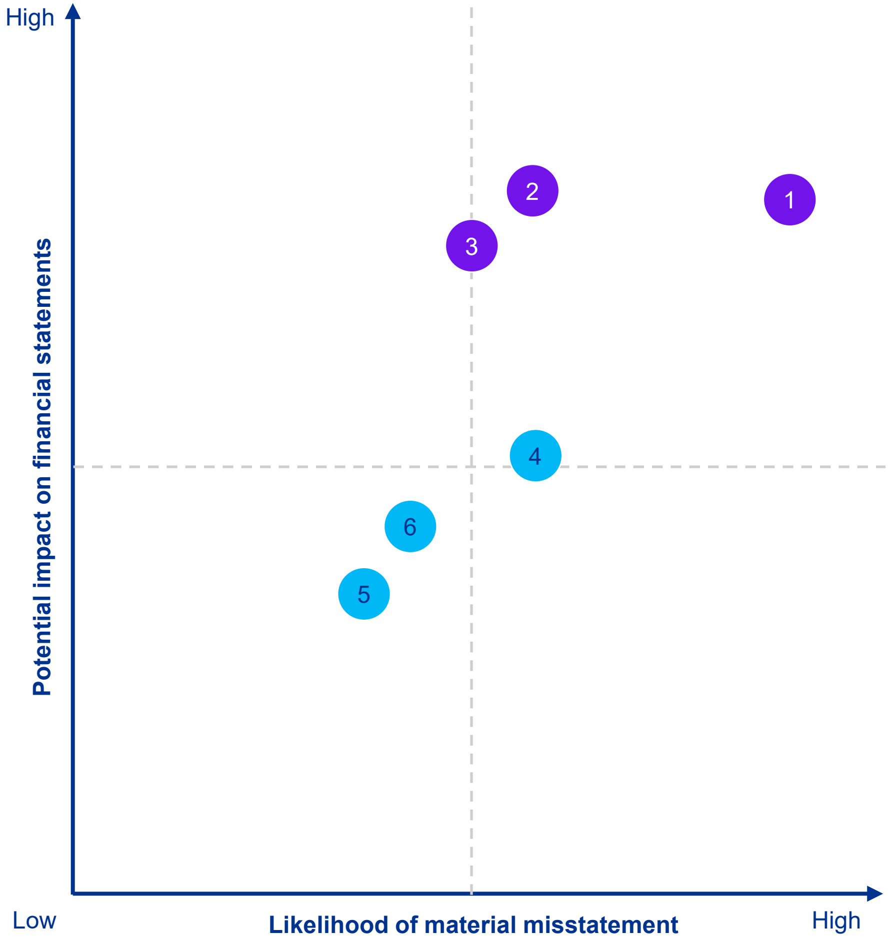
See the following slides for the cross-referenced risks identified on this slide.

Significant risks	
1.	Valuation of council dwellings
2.	Management override of controls
3.	Valuation of post retirement benefit obligations

Other audit risks	
4.	Expenditure recognition
5.	Transfer of services from Lewisham Homes
6.	Presentation of IFRS 16 pre-transition disclosure

Key: # Significant financial statement audit risks

Other audit risk



DRAFT

Audit risks and our audit approach

1 Valuation of council dwellings

The carrying amount of revalued land & buildings differs materially from the fair value

Cautious | Neutral | Optimistic

Significant audit risk

- 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 revaluation model which sees all land and buildings revalued each year, and Council Dwellings revalued in full on a five year rolling cycle, with indexation in intermediate years.
- This creates a risk that the carrying value of assets not revalued in year differs materially from the year end fair value.
- A further risk is presented for those assets that are revalued in the year, which involves significant judgement and estimation on behalf of the external valuer Wilks Head and Eve.
- The value of the Council's land and buildings at 31 March 2024 was £2,567m.
- This is on account of the judgement involved in the selection of assumption including, but not limited to:
  - Identification of assets as specialised or non-specialised; and
  - Obsolescence adjustments.
- We met with the Authority's valuers to understand their methodology and approach to valuation assumptions. Therefore we have revisited this risk throughout our audit once we have gained a deeper understanding of the approach.

Our response

We have performed the following procedures designed to specifically address the significant risk associated with the valuation:

- We critically assessed the independence, objectivity and expertise of Wilks Head and Eve, the valuers used in developing the valuation of the Authority's properties at 31 March 2024;
- We inspected the instructions issued to the valuers for the valuation of land and buildings to verify they are appropriate to produce a valuation consistent with the requirements of the CIPFA Code.
- We evaluated the design and implementation of controls in place for management to review the valuation and the appropriateness of assumptions used;
- We challenged the appropriateness of the valuation of council dwellings; including any material movements from the previous revaluations. We challenged key assumptions within the valuation as part of our judgement;
- We agreed the calculations performed of the movements in value of council dwellings and verified that these have been accurately accounted for in line with the requirements of the CIPFA Code; and
- Disclosures: We considered the adequacy of the disclosures concerning the key judgements and degree of estimation involved in arriving at the valuation.

We have performed the following other procedures within our work over the land and building balances:

- We compared the accuracy of the data provided to the valuers for the development of the valuation to underlying information.

DRAFT

Audit risks and our audit approach

1 Valuation of council dwellings

The carrying amount of revalued Land & Buildings differs materially from the fair value

Cautious | Neutral | Optimistic

Significant audit risk

- 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 revaluation model which sees all land and buildings revalued each year, and Council Dwellings revalued in full on a five year rolling cycle, with indexation in intermediate years.
- This creates a risk that the carrying value of assets not revalued in year differs materially from the year end fair value.
- A further risk is presented for those assets that are revalued in the year, which involves significant judgement and estimation on behalf of the external valuer Wilks Head and Eve.
- The value of the Council’s land and buildings at 31 March 2024 was £2,567m.
- This is on account of the judgement involved in the selection of assumption including, but not limited to:
  - Identification of assets as specialised or non-specialised; and
  - Obsolescence adjustments.
- We met with the Authority’s valuers to understand their methodology and approach to valuation assumptions. Therefore we have revisited this risk throughout our audit once we have gained a deeper understanding of the approach.

Our response

- Our assessment of management expert Wilks Head and Eve found them to be independent, objective, of appropriate expertise, and that instructions issued for the valuation were appropriate.
- We have identified a control deficiency regarding management review of the building valuation assumptions, because we did not identify a control to be assessed as a management review control in line with the auditing standards.
- It was identified by the management specialist that the valuation of council dwellings was materially incorrect due to index movements between January and March 2024, with a movement of £23.2m. The management specialist provided an updated valuation. This has been corrected by management.
- The key assumption in the valuation is how the appropriate EUV-SH methodology has been applied. We have validated values against sales data and support for property type with no issues identified in our testing to date.
- We identified a presentational error to the property numbers disclosure which has been corrected by management.
- We have agreed the journals posted for valuation movements in year to the financial statements. We will reconfirm the figures posted after audit adjustments are posted to the general ledger.

In addition to our response over the significant risk our work also highlighted the following findings:

- We identified a presentational misstatement in relation to the derecognition of Decent Homes expenditure. The expenditure is capitalised by the Authority and immediately derecognised within the land and buildings disclosures. We are of the view that this should be treated as an impairment. Presentation of the item should be moved within the HRA statement to reflect this treatment.
- During our audit testing it was identified that the floor area used in the valuation for one school was incorrect. Wilks Head and Eve have corrected for this in their valuation and it has been corrected in the financial statements by management.
- Our work over the valuation of land and buildings is substantially complete.

DRAFT

Audit risks and our audit approach (cont.)

2 Management override of controls[a]

Fraud risk related to unpredictable way management override of controls may occur

Significant audit risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant.
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.
- We have identified a specific risk of management override of controls in relation to HRA reserves. The reserves balance has fallen significantly over the past three years, and are under pressure due to demand. As the Authority is not permitted to be in a HRA deficit there is an increased risk of management override because of the motivation to understate HRA expenditure, specifically within the special expenses and repairs and maintenance balances.

Our response

- Our audit methodology incorporates the risk of management override as a default significant risk.
- Assessed accounting estimates for biases by evaluating whether judgements and decisions in making accounting estimates, even if individually reasonable, indicate a possible bias.
- Evaluated the selection and application of accounting policies.
- In line with our methodology, evaluated the design and implementation of controls over journal entries and post closing adjustments.
- Assessed the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates.
- Assessed the business rationale and the appropriateness of the accounting for significant transactions that are outside the entities normal course of business, or are otherwise unusual.
- We analysed all journals through the year using data and analytics and focus our testing on those with a higher risk, such as material journals posted during the final close down period, and unexpected account code combinations which reduce HRA expenditure balances and increase general fund balances.

Note: (a) Significant risk that professional standards require us to assess in all cases.

DRAFT

Audit risks and our audit approach (cont.)

2 Management override of controls[a] (cont.)

Fraud risk related to unpredictable way management override of controls may occur

Significant audit risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant.
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.
- We have identified a specific risk of management override of controls in relation to HRA reserves. The reserves balance has fallen significantly over the past three years, and are under pressure due to demand. As the Authority is not permitted to be in a HRA deficit there is an increased risk of management override because of the motivation to understate HRA expenditure, specifically within the special expenses and repairs and maintenance balances.

Our findings

- We identified 14 journal entries and other adjustments meeting our high-risk criteria – our examination did not identify unauthorised, unsupported or inappropriate entries.
- We evaluated the valuation of land and buildings and the valuation of the net pension liability, including the consideration of market movement data and did not identify any indicators of management bias. See slides 19 and 20 for further discussion.
- Our procedures did not identify any significant unusual transactions.
- We have not identified any control deficiencies in relation to the segregation of duties control.
- Our testing over journals is substantially complete. There are three journals outstanding in our testing.

Note: (a) Significant risk that professional standards require us to assess in all cases.

DRAFT

Audit risks and our audit approach (cont.)

3 Valuation of post retirement benefit obligations

An inappropriate amount is estimated and recorded for the defined benefit obligation

Cautious | Neutral | Optimistic

Significant audit risk

- The valuation of the post retirement benefit obligations involves the selection of appropriate actuarial assumptions, most notably the discount rate applied to the scheme liabilities, inflation rates and mortality rates. The selection of these assumptions is inherently subjective and small changes in the assumptions and estimates used to value the Authority's pension liability could have a significant effect on the financial position of the Authority.
- The effect of these matters is that, as part of our risk assessment, we determined that post retirement benefits obligation has a high degree of estimation uncertainty. The financial statements disclose the assumptions used by the Authority in completing the year end valuation of the pension deficit and the year on year movements.
- We have identified this in relation to the following pension scheme memberships: Local Government Pension Scheme (London Borough of Lewisham Pension Fund).
- Recent changes to market conditions have meant that more councils are finding themselves moving into surplus in their Local Government Pension Scheme (or surpluses have grown and have become material). In 2022-23 Lewisham recognised an asset for their defined benefit pension scheme of £3m and a liability of £142.2m. The requirements of the accounting standards on recognition of these surplus are complicated and requires actuarial involvement.

Our response

We have performed the following procedures :

- Understood the processes the Authority have in place to set the assumptions used in the valuation;
- Evaluated the competency, objectivity of the actuaries to confirm their qualifications and the basis for their calculations;
- Performed inquiries of the accounting actuaries to assess the methodology and key assumptions made, including actual figures where estimates have been used by the actuaries, such as the rate of return on pension fund assets;
- Agreed the input data provided by the audited entity to the actuaries for use within the calculation of the scheme valuation;
- Evaluated the design and implementation of controls in place for the Authority to determine the appropriateness of the assumptions used by the actuaries in valuing the liability;
- Challenged, with the support of our own actuarial specialists, the key assumptions applied, being the discount rate, inflation rate and mortality/life expectancy against externally derived data;
- Confirmed that the accounting treatment and entries applied by the Group are in line with IFRS and the CIPFA Code of Practice;
- Considered the adequacy of the Authority's disclosures in respect of the sensitivity of the deficit or surplus to these assumptions;
- Where applicable, assessed the level of surplus that should be recognised by the entity; and
- Assessed the impact of a last triennial valuation model and/or any special events, where applicable.

DRAFT

Audit risks and our audit approach (cont.)

3 Valuation of post retirement benefit obligations (cont.)

An inappropriate amount is estimated and recorded for the defined benefit obligation

Cautious Neutral Optimistic

Significant audit risk

- The valuation of the post retirement benefit obligations involves the selection of appropriate actuarial assumptions, most notably the discount rate applied to the scheme liabilities, inflation rates and mortality rates. The selection of these assumptions is inherently subjective and small changes in the assumptions and estimates used to value the Authority's pension liability could have a significant effect on the financial position of the Authority.
- The effect of these matters is that, as part of our risk assessment, we determined that post retirement benefits obligation has a high degree of estimation uncertainty. The financial statements disclose the assumptions used by the Authority in completing the year end valuation of the pension deficit and the year on year movements.
- We have identified this in relation to the following pension scheme memberships: Local Government Pension Scheme (London Borough of Lewisham Pension Fund).
- Recent changes to market conditions have meant that more councils are finding themselves moving into surplus in their Local Government Pension Scheme (or surpluses have grown and have become material). In 2022-23 Lewisham recognised an asset for their defined benefit pension scheme of £3m and a liability of £142.2m. The requirements of the accounting standards on recognition of these surplus are complicated and requires actuarial involvement.

Our findings

We have the following audit findings to report to you:

- We are mandated to consider the design of controls around approval of the pensions assumptions because these relate to a significant audit risk. The control currently in place is considered to be a management review control ('MRC'). Such controls are now subject to enhanced scrutiny by auditors and must comply with a series of prescriptive criteria in order to be considered effective. From discussion with management, it has been determined that although the actuarial assumptions are assessed on a high level, the review is not performed on a detailed enough basis to reliably and consistently address the risk that the assumptions used in the valuation may not be appropriate. Additionally, management do not produce control documentation to evidence the performance of this review, therefore the MRC has been deemed ineffective.
- We evaluated the capability, competency and objectivity of the actuaries to confirm their qualifications and the basis for their work with no issues noted. Also, basis inquiries performed with LGPS Actuaries, no unusual transactions were noted.
- We have verified the contributions data which is used within the calculation of the scheme valuation by obtaining the direct confirmation from auditor's of the pension fund and noted no issues.
- We considered that the assumptions used in valuing the defined benefit obligation and concluded overall to be balanced compared to our central actuarial benchmarks. See page 14 for details.
- Individually all assumptions are balanced except mortality future improvements, which is considered as cautious but within reasonable range. This is mainly because management specialist considered 1.50% as long term trend rate as compared to our central rate of 1.25%.

DRAFT

Audit risks and our audit approach (cont.)

3 Valuation of post retirement benefit obligations (cont.)

An inappropriate amount is estimated and recorded for the defined benefit obligation

Cautious Neutral Optimistic

Significant audit risk

- The valuation of the post retirement benefit obligations involves the selection of appropriate actuarial assumptions, most notably the discount rate applied to the scheme liabilities, inflation rates and mortality rates. The selection of these assumptions is inherently subjective and small changes in the assumptions and estimates used to value the Authority's pension liability could have a significant effect on the financial position of the Authority.
- The effect of these matters is that, as part of our risk assessment, we determined that post retirement benefits obligation has a high degree of estimation uncertainty. The financial statements disclose the assumptions used by the Authority in completing the year end valuation of the pension deficit and the year on year movements.
- We have identified this in relation to the following pension scheme memberships: Local Government Pension Scheme (London Borough of Lewisham Pension Fund).
- Recent changes to market conditions have meant that more councils are finding themselves moving into surplus in their Local Government Pension Scheme (or surpluses have grown and have become material). In 2022-23 Lewisham recognised an asset for their defined benefit pension scheme of £3m and a liability of £142.2m. The requirements of the accounting standards on recognition of these surplus are complicated and requires actuarial involvement.

Our findings

- There is no change in methodology while setting the actuarial assumptions except for mortality, which is set in line with the most recent triennial funding valuation and allowance for future improvement has been updated from CMI 2021 model to the CMI 2022 model to reflect the latest available industry data. Our actuaries have assessed the change and believe it is reasonable.
- Authority proposed to restrict the entire surplus to nil. We agree with the restriction of the surplus on the grounds that the estimated future service cost in each period, less the estimated minimum funding contributions for future service in those period as per IFRIC 14.20(b). This results in an additional liability of net £14,198k plus unfunded liability of £45,311k being recognised at 31 March 2024.
- During the year, the staff of, and services delivered by, Lewisham Homes were insourced back into the Authority. Following the decision by the Authority all employees were transferred under TUPE back to the Authority by 1st of October 2023, including their past service LGPS membership (which has been included in the DBO and Asset values at 31 March 2024 for the Authority). It is proposed to treat the event as a direct adjustment to the reserves with no impact on the comprehensive expenditure & income statement, a this was a transfer between associated Group entities. Our Actuary specialist has verified the reasonability of the accounting treatment and considered the values recognised for the transactions as materially correct. It resulted in an immediate net adjustment to reserves of £49,117k. However, based on the application of IFRIC 14 for both the Authority and Lewisham Homes, no surplus can be recognised and therefore a corresponding loss was recognised in other comprehensive income, meaning that the net surplus and net impact both are nil at the time of transfer.

DRAFT

Audit risks and our audit approach (cont.)

3 Valuation of post retirement benefit obligations (cont.)

An inappropriate amount is estimated and recorded for the defined benefit obligation

Cautious Neutral Optimistic

Significant audit risk

- The valuation of the post retirement benefit obligations involves the selection of appropriate actuarial assumptions, most notably the discount rate applied to the scheme liabilities, inflation rates and mortality rates. The selection of these assumptions is inherently subjective and small changes in the assumptions and estimates used to value the Authority's pension liability could have a significant effect on the financial position of the Authority.
- The effect of these matters is that, as part of our risk assessment, we determined that post retirement benefits obligation has a high degree of estimation uncertainty. The financial statements disclose the assumptions used by the Authority in completing the year end valuation of the pension deficit and the year on year movements.
- We have identified this in relation to the following pension scheme memberships: Local Government Pension Scheme (London Borough of Lewisham Pension Fund).
- Recent changes to market conditions have meant that more councils are finding themselves moving into surplus in their Local Government Pension Scheme (or surpluses have grown and have become material). In 2022-23 Lewisham recognised an asset for their defined benefit pension scheme of £3m and a liability of £142.2m. The requirements of the accounting standards on recognition of these surplus are complicated and requires actuarial involvement.

Our findings

- The Actuarial Funding Valuation for Fund, with an effective valuation date of 31 March 2022, was completed and signed on 28 March 2024. Given this is the first year of audit for KPMG, we have considered the following areas and noted no issues:
  - Funding position and agreed contributions
  - Areas of uncertainty around data or benefits
  - Valuation adjustments
- Below work is in progress:
  - Verifying the completeness, existence and accuracy of benefits paid, as we await confirmation from fund actuary.
  - We have reviewed the accounting treatment for the pension obligation/reimbursement right in relation to Lewisham Homes for the prior year and current year. Our work to conclude on the appropriateness of this treatment is ongoing.

DRAFT

Audit risks and our audit approach (cont.)

3 Valuation of post retirement benefit obligations (cont.)

An inappropriate amount is estimated and recorded for the defined benefit obligation

Level of prudence compared to KPMG central assumptions

Audit misstatement | *Cautious* | *Balanced* | *Optimistic* | *Audit misstatement*

Reasonable range

Overall assessment of assumptions for audit consideration							*Balanced*	
Underlying assessment of individual assumptions		**Methodology**	**Consistent methodology to prior year?**	**Compliant methodology with accounting standard?**	**Employer**	**KPMG central**	**Assessment**	**Significant assumption**
Discount rate		AA yield curve	✓	✓	4.80%	4.81%	Balanced	✓
CPI inflation		Deduction to inflation curve with adjustment for recent inflation experience	✓	✓	2.80%	2.85%	Balanced	✓
Pension increases		In line with CPI	✓	✓	2.80%	2.88%	Balanced	
Salary increases		CPI + 1%, In line with most recent Fund valuation	✓	✓	3.80%	In line with long-term remuneration policy	Balanced	
Mortality	Base tables	In line with most recent Fund valuation	✓	✓	Fund-specific based on Club Vita Curves	In line with best-estimate Fund experience	Balanced	✓
	Future improvements	In line with most recent Fund valuation, updated to use latest CMI model	✓	✓	CMI 2022 projections model, 1.5% long-term trend rate, initial addition parameter of 0.25% and default other parameters	CMI 2022,1.25% long-term trend rate and default other parameters	Cautious	✓
Other demographics		In line with most recent Fund valuation	✓	✓	Member can take 50% of the maximum additional tax-free cash up to HMRC limits	In line with Fund experience	Balanced	

DRAFT

Audit risks and our audit approach (cont.)

4 Risk of error from expenditure recognition

Liabilities and related expenses for purchases of goods or services are not completely and accurately identified and recorded

Other audit risk

- Whilst the Authority is faced with increasing demand for services the financial position of the Authority, whilst under pressure in specific areas, is not indicative of a position that would provide an incentive to manipulate expenditure recognition.
- We have therefore rebutted the presumed fraud risk over expenditure recognition (see page 12 of our Audit Plan).
- We have retained a risk of error due to the directorate structure of the Authority and the decentralised approach to processing year-end accruals.

Our response

We have performed the following procedures in order to respond to the other risk identified:

- We inspected a sample of invoices of expenditure, in the period around 31 March 2024, to determine whether expenditure has been recognised in the correct accounting period and whether accruals are complete;
- We selected a sample of year end accruals and inspected evidence of the actual amount paid after year end in order to assess whether the accruals have been accurately recorded; and
- We compared the items that were accrued at 31 March 2023 to those accrued at 31 March 2024 in order to assess whether any items of expenditure not accrued for as at 31 March 2024 have been done so appropriately.

DRAFT

Audit risks and our audit approach (cont.)

4 Risk of error from expenditure recognition (cont.)

Liabilities and related expenses for purchases of goods or services are not completely and accurately identified and recorded

Other audit risk

- Whilst the Authority is faced with increasing demand for services the financial position of the Authority, whilst under pressure in specific areas, is not indicative of a position that would provide an incentive to manipulate expenditure recognition.
- We have therefore rebutted the presumed fraud risk over expenditure recognition (see page 12 of our Audit Plan).
- We have retained a risk of error due to the directorate structure of the Authority and the decentralised approach to processing year-end accruals.

Our findings

- Our testing of accruals and expenditure is complete.
- Our cut-off testing did not identify any non-pay expenditure which had been recorded in the incorrect period.
- We identified two corrected audit misstatements. This was a presentational adjustment between income and expenditure, and a correction to an accrual which had not been reversed in previous years was identified in our accruals sample testing.
- Our comparison of current year to prior year accruals did not identify any differences which could not be corroborated.

DRAFT

Audit risks and our audit approach (cont.)

5 Transfer of services from Lewisham Homes

Liabilities and related expenses for purchase of goods or services are not completely identified and recorded

Other audit risk

- As at 1 October 2023 a large proportion of the services in Lewisham Homes Limited have transferred to the London Borough of Lewisham.
- The Authority will reflect the net pension liabilities in the balance sheet at the year-end as well as reflecting the relevant staff costs, income and expenditure from the date of transfer.
- To facilitate the transfer, data from Lewisham Homes Limited's finance systems has been transferred to the Authority. This includes, but is not limited to, records of staff, and historic records of fixed assets including cost, revaluations and depreciation to date.
- Data has been manually transferred.
- Therefore, there is a risk that the transfer of data has not been completely and accurately recorded.

Our response

We have performed the following procedures:

- We have drawn on support from KPMG IT Audit team members to support the audit team in understanding the systems involved in the transfer of data, and related risks;
- We have performed inquiry of management to understand the reconciliation process performed at the date of transfer of data to the Authority, and how agreements have been reached on the balances to transfer. This also included a walk through of the process, to understand the controls in place.
- We have obtained journals used to transfer the relevant balance sheet items from Lewisham Homes Limited financial statements and confirmed that they have been completely transferred.

We are still to complete:

- We have selected a sample of income and expenditure items from the month before and month after the transfer date of 1 October 2023, and confirmed that the items related to Lewisham Homes Limited activity have been recorded in the correct accounting period.

DRAFT

Audit risks and our audit approach (cont.)

5 Transfer of services from Lewisham Homes

Liabilities and related expenses for purchases of goods or services are not completely identified and recorded

Other audit risk

- As at 1 October 2023 a large proportion of the services in Lewisham Homes Limited have transferred to the London Borough of Lewisham.
- The Authority will reflect the net pension liabilities in the balance sheet at the year-end as well as reflecting the relevant staff costs, income and expenditure from the date of transfer.
- To facilitate the transfer, data from Lewisham Homes Limited’s finance systems has been transferred to the Authority. This includes, but is not limited to, records of staff, and historic records of fixed assets including cost, revaluations and depreciation to date.
- Data has been manually transferred.
- Therefore, there is a risk that the transfer of data has not been completely and accurately recorded.

Our findings

- During our audit procedures we identified difficulties with obtaining information from Lewisham Homes, due to detailed records not being maintained and documents not being saved after the transfer of activities to the Authority. We have performed alternative procedures for our audit to obtain sufficient, appropriate audit evidence.
- We have considered this within our Value for Money risk assessment, which is in progress.

DRAFT

Audit risks and our audit approach (cont.)

6 Presentation of IFRS 16 pre-transition disclosures

Risk of error related to the incorrect presentation of disclosures for the implementation of the IFRS 16 leases standard

Other audit risk

- In accordance with the CIPFA Code, the Authority is required to adopt IFRS 16 Leases from the 31 March 2025 year-end.
- The Code requires that the Authority produces either quantitative or qualitative disclosures in the 31 March 2024 financial statements setting out the anticipated impact of the transition to IFRS 16.
- Under the new standard, the Authority will be required to recognise right of use assets and lease liabilities relating to operating leases which are currently held off balance sheet. There are also changes to the accounting of finance leases but there is less impact compared to the operating leases because finance leases are already held on balance sheet.
- Whilst the value of the operating leases is small (at 31 March 2023, the future minimum lease payments were under £19m), the new disclosures related to the transition to the new standard are risky because:
  - The Authority has not previously been required to prepare this kind of disclosure before;
  - There can be difficulties in establishing the completeness of the list of assets; and
  - There are complexities in the identification of leases that are affected, including peppercorn leases.

Our response

- We have performed the following procedures:
  - Inquiry of management to understand whether the entity intends to prepare quantitative (and if so, the value) or qualitative disclosures;
  - Inquired of management to understand how the Authority plans to transition to IFRS 16, and assess whether the transition plan is appropriate; and
  - Assessed whether the disclosures made are in line with the CIPA Code, our understanding o the Authority, and the transition plan described to us by management.

DRAFT

Audit risks and our audit approach (cont.)

6 Presentation of IFRS 16 pre-transition disclosures

Risk of error related to the incorrect presentation of disclosures for the implementation of the IFRS 16 Leases standard

Other audit risk

- In accordance with the CIPFA Code, the Authority is required to adopt IFRS 16 Leases from the 31 March 2025 year-end.
- The Code requires that the Authority produces either quantitative or qualitative disclosures in the 31 March 2024 financial statements setting out the anticipated impact of the transition to IFRS 16.
- Under the new standard, the Authority will be required to recognise right of use assets and lease liabilities relating to operating leases which are currently held off balance sheet. There are also changes to the accounting of finance leases but there is less impact compared to the operating leases because finance leases are already held on balance sheet.
- Whilst the value of the operating leases is small (at 31 March 2023, the future minimum lease payments were under £19m), the new disclosures related to the transition to the new standard are risky because:
  - The Authority has not previously been required to prepare this kind of disclosure before;
  - There can be difficulties in establishing the completeness of the list of assets; and
  - There are complexities in the identification of leases that are affected, including peppercorn leases.

Our findings

- The Authority has not included complete IFRS 16 pre-transition disclosures in the draft financial statements Whilst they have included acknowledgement of the upcoming change in the standard, according to IAS 8, the disclosure should include a discussion of the estimated impact the introduction of new standards will have on the financial statements. If a reasonable estimate cannot be made due to data limitations, this fact should be disclosed.

  While the lack of quantitative disclosures in the 2023-24 financial statements is not considered an omission, given the standard's effective date of April 1, 2024, it is expected that management should be well advanced In their quantitative impact assessment for the 2024-25 financial statements.

  There is a risk that delaying this assessment could lead to errors, insufficient review time, and potentially material misstatements. Management should ensure that the quantitative impact assessment is schedules and completed promptly, allowing sufficient time for review and challenge before positing transition adjustments.

  Our work to assess this is ongoing.

DRAFT

Key accounting estimates and management judgements – overview

Our view of management judgement

Our views on management judgments with respect to accounting estimates are based solely on the work performed in the context of our audit of the financial statements as a whole. We express no assurance on individual financial statement captions.

Asset/liability class	Our view of management judgement (Cautious / Neutral / Optimistic)	Balance (£m)	YoY change (£m)	Our view of disclosure of judgements & estimates (Needs improvement / Neutral / Best practice)	Further comments
Valuation of Council Dwellings	Neutral	2,567	86	Neutral	We identified three audit misstatements in relation to the valuation of land and buildings, being a presentational misstatement in relation to the derecognition of Decent Homes expenditure, an update to the valuation due to large index movements between January and March 2024 and it was identified that the floor area used in the valuation for one school was incorrect. All audit misstatements have been corrected by management. We have identified a control deficiency regarding management review of the building valuation assumptions. Our work over the assumptions underlying the valuation has not identified any other significant differences compared to our expectations.

DRAFT

Key accounting estimates and management judgements – overview

Our view of management judgement

Our views on management judgments with respect to accounting estimates are based solely on the work performed in the context of our audit of the financial statements as a whole. We express no assurance on individual financial statement captions.

Asset/liability class	Our view of management judgement	Balance (£m)	YoY change (£m)	Our view of disclosure of judgements & estimates	Further comments
Valuation of defined benefit obligation (gross)	Cautious / Neutral / Optimistic: Neutral	1,873	274	Needs improvement / Neutral / Best practice: Neutral	We have assessed the accounting results, including the individual balance sheet, P&L, OCI elements and the sensitivity of the Defined Benefit Obligation (DBO) to changes in key assumptions. Overall, the DBO estimate has been found to be balanced.

Other significant matters

Control deficiencies

We obtain an understanding of internal control to design appropriate audit procedures, but not to express an opinion on the effectiveness of the Authority's internal control.

We did not identify any significant control deficiencies in our testing.

Significant difficulties

We have not encountered any matters which led to significant difficulties in performing the audit.

Quality and timeliness of information prepared by management/those charged with governance

In our view, the quality of information:

- supported our ability to understand key decisions better and obtain sufficient audit evidence
- enabled informed challenge of management decisions
- supported audit quality and better disclosure.

DRAFT

Significant audit misstatements

Management has approved the correction of the audit misstatements detailed on pages 42 and 43 and they are reflected in the draft financial statements. A summary of the uncorrected audit misstatements is detailed on page 41.

The misstatements identified, and their estimated financial impact on the deficit, are summarised in the table on the right.

The most significant disclosure misstatements relate to:

- the update of the PPE valuation to reflect updated index movements and one incorrect floor area used.

In line with ISA (UK) 450 we request that you correct uncorrected misstatements.

- If the uncorrected factual audit misstatements were posted, they would increase the deficit by £0.0m
- For our views on management estimates – see pages 21 and 22 (Key accounting estimates)
- A detailed summary of corrected and uncorrected audit misstatements and omissions and errors in disclosure is included in the appendix.

Audit misstatements - deficit

	Type	£m	Comment
Trial balance		83.1	
Corrected misstatements			
Movement in published PPE indices	Factual	0.0	
Floor areas adjustment to PPE valuation	Factual	0.0	
Reversal of prior period accrual	Factual	0.0	
De-recognition of Decent Homes expenditure	Factual	0.0	
Children's Social Care Accrual	Factual	0.0	
Reported in FS		83.1	
Uncorrected misstatements			
Nil	Factual	0.0	There are no uncorrected audit misstatements.
Our assessment		83.1	

Disclosure

Matter	IAS/IFRS ref	Comment
Property numbers	N/A	Misstatement due to incorrect disclosure

Types of misstatement

Factual: Misstatements about which there is no doubt

Projected: Our best estimate of misstatements in the audited populations

Judgemental: Differences arising from judgments of management that we consider unreasonable or inappropriate

DRAFT

Other matters

Narrative report

We are in the process of reading the contents of the Narrative Report and checking compliance with the requirements of the Annual Report and financial statements with the Code of Practice on Local Authority Accounting in the United Kingdom 2023/24 ('the Code'). Based on the work performed to date:

- We have not identified any inconsistencies between the contents of the Narrative Report and the financial statements.
- We have not identified any material inconsistencies between the knowledge acquired during our audit and the statements of the Council. As Audit and Risk Committee members you confirm that you consider that the Narrative Report and financial statements taken as a whole are fair, balanced and understandable and provides the information necessary for regulators and other stakeholders to assess the Council's performance, model and strategy.

However, our work in this area is not yet concluded.

Annual Governance Statement

We have reviewed the Council's 2023/24 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 and is consistent with other information we are aware of from our audit of the financial statements.

Whole of Government Accounts

As required by the National Audit Office (NAO) we carry out specified procedures on the Whole of Government Accounts (WGA) consolidation pack.

We have confirmed that, for London Borough of Lewisham, the threshold at which detailed testing is required has not been exceeded.

We will submit an updated assurance statement on completion of the audit and following review the final financial statements.

Independence and Objectivity

ISA 260 also requires us to make an annual declaration that we are in a position of sufficient independence and objectivity to act as your auditors, which we completed at planning and no further work or matters have arisen since then.

Audit Fees

Our PSAA proscribed 2023/24 audit scale fee for the audit was **£480,763** plus VAT.

We have also completed non audit work at the Authority during the year on Housing benefit grant certification and VAT and taxation services for Lewisham Homes, and have included in appendix 2 confirmation of safeguards that have been put in place to preserve our independence.

DRAFT

Subsidiary audits: Lewisham Homes

<table>
<tr><th>Entity</th><th>Reporting framework</th><th>Materiality</th><th>Significant risks</th></tr>
<tr><td>Lewisham Homes Limited</td><td>This company is required to produce accounts in accordance with the Companies Act 2006.

The accounts are produced in accordance with UK accounting standards, including FRS 102 The Financial Reporting Standard applicable in the UK and the Republic of Ireland.</td><td>We have determined an appropriate level of materiality for our audit of Lewisham Homes, using month 6 total revenues as the benchmark.

Materiality has been set at £0.7m (2022/23: £1.13m) which is approximately 2.0% of total revenues (2022/23: 2.0%).

We will design our procedures to detect individual errors above £455k (2022/23 £743k). We will report individual errors identified above £35k (2022/23: £56.5k).</td><td>Our audit methodology incorporates the risk of management override as a default significant risk. Our methodology considers journals, unusual transactions and any estimates/judgements made by management.

Other audit risks

We have identified an other audit risk over the transfer of data from Lewisham Homes Limited to London Borough of Lewisham. As at 1 October 2023 the services previously provided by Lewisham Homes have been brought in house by the Authority. This is expected to greatly reduce income, expenditure and staff costs for the second half of the financial year, as well as the net pension liabilities in the entity’s balance sheet. To facilitate the transfer, data from the entity's finance systems has been transferred to the Authority. This includes, but is not limited to, records of staff, and historic records of fixed assets including cost, revaluations and depreciation to date. Data has been manually transferred. Therefore, there is a risk that the transfer of data has not been completely and accurately recorded.

We have also identified an other audit risk over going concern. Management’s assessment of the entity’s ability to continue as a going concern involves significant judgement with respect to the future operations of the entity. There is a risk that management’s assessment of the entity’s ability to continue as a going concern does not appropriately consider the impact of the transfer of activities to London Borough of Lewisham and whether remaining operations will viably continue. There is also a risk that disclosures in the financial statements and annual report do not adequately reflect the effect on the entity’s performance, business model and strategy.

Rebuttal of revenue significant risk

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk and we have rebutted this risk for all revenue streams.

Management fee income is agreed in contract with simple recognition criteria linked to services delivered. The values are agreed with the Authority, with limited scope for manual intervention.

While income from rents could be received in advance or arrears it is a steady periodic amount of income. Overall the balance is not significant for the entity. The housing stock it relates to is non-complex and transactions are low in volume and complexity.

We do not deem there to be any incentive or opportunity to manipulate other income, including repairs and maintenance income and note there would need to be a significant volume of transactions misstated to create a material error. Due to the transfer of data to London Borough of Lewisham in months six we expect any cut-off differences to be resolved well in advance of the year end date.</td></tr>
</table>

DRAFT

Subsidiary audits: Lewisham Homes

<table>
<tr><th>Entity</th><th>Reporting framework</th><th>Materiality</th><th>Significant risks</th></tr>
<tr>
<td>Lewisham Homes Limited</td>
<td>This company is required to produce accounts in accordance with the Companies Act 2006.

The accounts are produced in accordance with UK accounting standards, including FRS 102 The Financial Reporting Standard applicable in the UK and the Republic of Ireland.</td>
<td>We have determined an appropriate level of materiality for our audit of Lewisham Homes, using month 6 total revenues as the benchmark.

Materiality has been set at £0.7m (2022/23: £1.13m) which is approximately 2.0% of total revenues (2022/23: 2.0%).

We will design our procedures to detect individual errors above £455k (2022/23 £743k). We will report individual errors identified above £35k (2022/23: £56.5k).</td>
<td>Response and Findings

We identified six audit misstatements in our audit of Lewisham Homes.

All identified audit misstatements have been corrected.

<table>
<tr><th colspan="5">Corrected audit differences (£'s)</th></tr>
<tr><th>No.</th><th>Detail</th><th>SOCI Dr/(cr)</th><th>SOFP Dr/(cr)</th><th>Comments</th></tr>
<tr><td>1</td><td>Dr Tax liability
Cr Accrued expenses</td><td>84,000</td><td>
(84,000)</td><td>A tax liability of £84k had not been processed through the general ledger.</td></tr>
</table>

We also identified the following presentational changes to the financial statements.

Interest payable had been incorrectly transposed between the trial balance and draft financial statements.
Presentational changes to the related parties disclosure to reflect missing related party transactions, and to remove related parties which no longer met the conditions to be reported.
Presentational changes to the narrative element of the staff numbers disclosure to be consistent with the numbers reported.
Presentational change to the number of leases shown in the lease disclosure.
Presentational changes to the property numbers disclosure to reflect the current year property numbers.

We identified four control deficiencies which have been outlined on the following pages.

Our work over going concern did not identify any material uncertainty and we have been able to conclude that the entity remains a going concern.

Our testing over Lewisham Homes is substantially complete.</td>
</tr>
</table>

DRAFT

Subsidiary audits: Lewisham Homes

The recommendations raised as a result of our work over Lewisham Homes in the current year are as follows:

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

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
1	❷	**Payroll controls** As a result of their transfer to Lewisham Council, management were unable to provide pre-transfer documents for payroll controls including amendment forms and a breakdown of amendments. The Authority should satisfy itself over whether the transferred payroll data from Lewisham Homes is complete and accurate. Lewisham Homes should ensure that they have revisited their document retention policies and designed an appropriate method for storing and retention of key documents.	
2	❷	**Related party disclosure forms** Disclosure forms had not been obtained for two new Directors, and the process for updating declarations was not completed in 2023-24. There is a risk that related party transactions are missed where information is not up to date. We recommend management perform a full refresh of declarations for the next financial year. We also recommend they revisit their process for obtaining updated declarations to ensure there is accountability for incomplete declarations with appropriate follow-up.	

DRAFT

Subsidiary audits: Lewisham Homes

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

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
3	2	**Undeclared Director interests** We identified three directors who had interests on Companies House that were not included on the declarations of interest. We recommend that management include within their annual declaration process a reminder to Directors on the importance of a complete declaration, guidance on what should be included, and a check to Companies House and other public information.	
4	2	**Journals segregation of duties** During the understanding of the journals process, we noted that the approver/authoriser of the journal can change key elements of the journal, therefore increasing the risk of fraudulent journals being processed. We further note that there are system limitations which prevents the approver from notifying any changes requested on the journal and sending back to the capturer to subsequently correct. We do note, that Lewisham Homes does have a policy in place which requires that any changes requested by the approver of the journal, is requested to be made by the capturer of the journal, however, no records of logs are kept for journals changes before authorising. There is also the possibility of having the same poster and approver which was noted from our Journals HRC screening. We recommend that management implements system changes to prevent the approver from having access to make changes to the journal without the capturer of the journal in order to eliminate the risk of fraudulent journals being processed.	

02
London Borough of Lewisham Value for Money

Year ended 31 March 2024

—

12 December 2024

Value for money

We are required under the Audit Code of Practice to confirm whether we have identified any significant weaknesses in the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources.

In discharging these responsibilities we include a statement within the opinion on your accounts to confirm whether we have identified any significant weaknesses. We also prepare a commentary on your arrangements that is included within our Auditor's Annual Report, which is required to be published on your website alongside your annual report and accounts.

Commentary on arrangements

We have not yet finalised our commentary on the your arrangements. However we will complete our value for money procedures prior to signing of the financial statements opinion in January 2025. The report is required to be published on your website alongside the publication of the annual report and accounts.

Response to risks of significant weaknesses in arrangements to secure value for money

As noted on the right, we have identified two risks of a significant weakness in the Authority's arrangements to secure value for money. Within our draft Auditor's Annual Report we have set out our response to those risks.

Summary of findings

We have set out in the table below the outcomes from our risk assessment procedures against each of the domains of value for money:

Domain	Risk assessment
Financial sustainability	One significant risk identified
Governance	One significant risk identified
Improving economy, efficiency and effectiveness	No significant risks identified.

Further detail will be set out in our Auditor's Annual Report.

Significant value for money risks

1 Sustainability of Housing Revenue Account

Risk that value for money arrangements may contain a significant weakness linked to the domain of financial sustainability

Significant Value for Money Risk

Description

Our risk assessment procedures identified pressure on the Authority's housing directorate. Lewisham has a large social housing portfolio and consequently its housing directorate needs to respond to a variety of pressures and issues, such as overspending against the repairs budget and new regulations including building safety, fire, damp and mould.

A key risk we identified relates to financial sustainability of the Housing Revenue Account. Availability of financial resources is key to ensuring that homes can be well maintained and that the service can operate effectively.

During 2023/24, the HRA budget was overspent by £6.1m. Lewisham's HRA has been experiencing financial pressures caused by (amongst other factors) inflation, new building safety obligations, below-inflation rent increase caps, and overspending against the repairs budget. There is also additional pressure on the HRA as a result of the self-referral to the Regulator of Social Housing, resulting in a large proportion of housing stock being identified as below the Decent Homes standard and requiring works. The value of reserves in the HRA has been falling over time, which reduces the ability of the Authority to respond to unexpected cost pressures. At 31 March 2024, the HRA reserve stood at £7.4m, a reduction of £6.7m since the prior period. The Authority has developed a 30-year Business Plan as well as a Repairs Transformation Project to restore the financial sustainability of the HRA.

The low value of the HRA reserve, combined with the overspend during 2023/24 raises the risk that there were no adequate arrangements in place in 2023/24 in relation to the financial sustainability of the HRA.

Our response

Response

We will perform the following procedures:

- Evaluate the factors causing the HRA overspend during 2023/24, and assess whether there were appropriate arrangements to monitor and control spending during the year.
- Obtain and read the 30-year HRA Business Plan. Assess whether the plan was subject to appropriate review, challenge, and approval prior to coming into force.
- Ensure the 30-year HRA Business Plan is plausible in reference to forecast interest and inflation rates; new building safety regulations; and capital expenditure required in respect of stock condition and known capital commitments.

Our work in this area is ongoing.

Significant value for money risks

2 Social housing stock and remediation plans

Risk that value for money arrangements may contain a significant weakness linked to the domain of governance

Significant Value for Money Risk

Description

The Authority self-referred to the Regulator of Social Housing in December 2023 due to identifying a failure to meet statutory health and safety requirements in some of its homes, including overdue fire remedial actions and repairs. The regulator concluded that the Authority is not meeting the required outcomes of the Decent Homes Standard but there is no statutory or enforcement action that they have taken to date.

The Authority have contracted Savills to undertake a full stock condition survey and plan to address non-decency, fire remedial actions and repairs. So far, the stock condition survey has identified around 24% of homes not in line with the Decent Homes standard as reported to the Regulator in the Lewisham Authority Regulatory report November 2024, but this may increase on completion of the survey. The completion of the works required to meet the Decent Homes standard will also put additional pressure on HRA reserves which are already under significant pressure.

The Authority reports to the Regulator on a regular basis with an update on the work completed to date to remediate the issues identified, including responsive repairs performance, movement on fire safety actions and an update on the stock condition survey programme. The Authority also has a Repairs Improvement Plan which is regularly updated.

We have therefore identified a significant risk that the Authority may not have appropriate governance arrangements in place in relation to social housing stock and remediation plans.

Our response

Response

We will perform the following procedures:

- Obtain an understanding of the escalation process that led to the self-referral
- Obtain and review the monitoring reports the Council have shared with the Regulator
- Obtain and review the programme the Council have put in place to rectify the issues identified as a result of the self-referral to the Regulator
- Obtain and review the draft Savills stock condition survey
- Obtain and review the Repairs Improvement Plan
- Assess the ongoing monitoring arrangement of housing stock condition and the associated reporting mechanisms.

Our work in this area is ongoing.

03
London Borough of Lewisham Appendices

Year ended 31 March 2024

—

12 December 2024

Appendices

Contents	Page

DRAFT

Required communications

Type	Response
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 2024.
Adjusted audit differences	There were five adjusted audit differences with a surplus impact of £nil. See page 24.
Unadjusted audit differences	The aggregated surplus impact of unadjusted audit differences would be £0.0m. 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 page 24.
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 and Risk 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 communicated to management in writing all deficiencies in internal control over financial reporting of a lesser magnitude than significant deficiencies identified during the audit that had not previously been communicated in writing on 26 November 2024.
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts	No actual or suspected fraud involving group or /Authority management, employees with significant roles in internal control, or where fraud results in a material misstatement in the financial statements identified during the audit.
Make a referral to the regulator	If we identify that potential unlawful expenditure might be incurred then we are required to make a referral to your regulator. We have not identified any such matters.
Issue a report in the public interest	We are required to consider if we should issue a public interest report on any matters which come to our attention during the audit. We have not identified any such matters.

Type	Response
Significant difficulties	No significant difficulties were encountered during the audit.
Modifications to auditor's report	None
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.
Other information	No material inconsistencies were identified related to other information in the annual report, Strategic and Directors' reports. The Strategic report is fair, balanced and comprehensive, and complies with the law.
Breaches of independence	No matters to report. The engagement team and others in the firm, as appropriate and the firm have complied with relevant ethical requirements regarding independence.
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.
Significant matters discussed or subject to correspondence with management	None
Certify the audit as complete	Due to the Auditor's Annual Report being issued later in the year we have not yet certified the audit as complete. There are no other issues delaying this being issued.
Provide a statement to the NAO on your consolidation schedule	We will issue our report to the National Audit Office following the signing of the annual report and accounts.

Fees

Audit fee

Our fees for the year ending 31 March 2024 are set out in the PSAA Scale Fees communication and are shown below.

Entity	2023/24 (£'000)	*2022/23 (£'000)*
Statutory audit	481	*269[a]*
Lewisham Homes – statutory audit (base fee plus inflation)	78	75
Lewisham Homes – additional work required on transfer	16	-
ISA315r	16	-
ISA240	TBC	-
Other variations	TBC	
TOTAL	**591**	*344*

Note: (a) Fee charged by Grant Thornton – your predecessor auditor.

Billing arrangements

- Fees have been billed in accordance with the milestone completion phasing that has been communicated by the PSAA.
- As per PSAA's Scale Fees Consultation, the scale fees did not include new requirements of ISA315 revised (risk of material misstatement); or ISA 240 (auditor's responsibilities relating to fraud.
- Additional fees will be subject to the fees variation process as outlined by the PSAA.

Confirmation of Independence

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

To the Audit and Risk Committee members

Assessment of our objectivity and independence as auditor of London Borough of Lewisham

Professional ethical standards require us to provide to you at the planning stage 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.

This letter 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/directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. 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.

We are satisfied that our general procedures support our independence and objectivity except for those detailed below where additional safeguards are in place.

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

Summary of non-audit services

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 on the table overleaf.

DRAFT

Confirmation of Independence (cont.)

Disclosure	Description of scope of services	Principal threats to Independence	Safeguards Applied	Basis of fee	Value of services delivered in the year ended 31 March 2024 £	Value of services committed but not yet delivered £
1	Housing benefit grant certification	Management Self review Self interest	• Standard language on non-assumption of management responsibilities is included in our engagement letter. • The engagement contract makes clear that we will not perform any management functions. • The work is performed after the audit is completed and the work is not relied on within the audit file. • Our work does not involve judgement and are statements of fact based on agreed upon procedures.	Fixed	£35,000	nil
2	Lewisham Homes - Other assurance services (VAT and taxation)	Management Self review Self interest	• Work is performed by a team separate from the audit team. • Services do not result in any material judgements within the financial statements. • Management remain responsible for any decisions. • The audited statement has no impact on the year end accounts.	Fixed	£27,700	nil

Confirmation of Independence (cont.)

Summary of fees

We have considered the fees charged by us to the Group and its affiliates for professional services provided by us during the reporting period.

Fee ratio

The ratio of non-audit fees to audit fees for the year is anticipated to be 0.07: 1. We do not consider that the total non-audit fees create a self-interest threat since the absolute level of fees is not significant to our firm as a whole.

	2023/24
	£'000
Statutory audit (incl. ISA315R)	497
Audit of subsidiaries	94
Other assurance services – Housing Benefits	35
Other assurance services – Lewisham Homes	28
Total Fees	**654**

Application of the FRC Ethical Standard 2019

Your previous auditors will have communicated to you the effect of the application of the FRC Ethical Standard 2019. That standard became effective for the first period commencing on or after 15 March 2020, except for the restrictions on non-audit and additional services that became effective immediately at that date, subject to grandfathering provisions.

AGN 01 states that when the auditor provides non-audit services, the total fees for such services to the audited entity and its controlled entities in any one year should not exceed 70% of the total fee for all audit work carried out in respect of the audited entity and its controlled entities for that year.

We confirm that as at 15 March 2020 we were not providing any non-audit or additional services that required to be grandfathered.

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 and Risk Committee.

Confirmation of audit independence

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

This report is intended solely for the information of the Audit and Risk Committee of the Group 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.

Yours faithfully

KPMG LLP

DRAFT

Uncorrected audit misstatements

Under UK auditing standards (ISA (UK) 260) we are required to provide the Audit and Risk Committee with a summary of uncorrected audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements. In line with ISA (UK) 450 we request that you correct uncorrected misstatements. However, they will have no effect on the opinion in our auditor's report, individually or in aggregate. As communicated previously with the Audit and Risk Committee, details of all adjustments greater than £1,230K are shown below:

Uncorrected audit differences (£'000s)

There are no uncorrected audit differences.

Corrected audit misstatements

Under UK auditing standards (ISA (UK) 260) we are required to provide the Audit and Risk Committee with a summary of corrected audit differences (including disclosures) identified during the course of our audit. The adjustments below have been included in the financial statements.

Corrected audit differences (£'s)

No.	Detail	SOCI Dr/(cr)	SOFP Dr/(cr)	Comments
1	Dr Council Dwellings (PPE)	-	23,191,172.00	Wiks Head and Eve conduct their valuation as at 31st January 2024, and roll forward the valuation to 31st March 2024. Movement in the land registry indices in the period resulted in a material movement in the valuation. Therefore an updated valuation was provided.
	Dr Usable Capital Reserves	-	868,103.54	
	Dr Impairment	898,972.88	-	
	Cr MIRS	(898,972.88)	-	
	Cr Revaluation Reserve	-	(24,059,275.54)	
2	Dr Other Land and Buildings (PPE)	-	7,047,000.00	During our audit testing we identified that the floor areas used in the valuation for one school were incorrect. An adjustment was made to the valuation to reflect the correct floor areas.
	Cr Revaluation Reserve	-	(7,150,693.20)	
	Dr Impairment	103,693.20	-	
	Dr CAA	-	103,693.20	
	Cr MIRS	(103,693.20)	-	
3	Dr Creditors (Trade payables)	-	1,813,502.60	Invoices which were accrued in prior periods but were incorrectly not reversed in 22/23 were reversed during the current year.
	Cr HRA Reserve	-	(1,813,502.60)	
	Cr Gain or loss on disposal	(1,813,502.60)	-	
	Dr Transfer to reserves (HRA)	1,813,502.60	-	

DRAFT

Corrected audit misstatements (cont.)

Corrected audit differences (£'s)				
No.	**Detail**	**SOCI Dr/(cr)**	**SOFP Dr/(cr)**	**Comments**
4	Cr Gain or Loss on disposal	(65,365,189.16)	-	Decent Homes expenditure within the HRA disclosure to move the derecognition of capitalized expenditure to above the line.
	Dr Capital charges (HRA)	65,365,189.16	-	
5	Dr Other expenditure (CYP)	2,617,089.00	-	Adjustment identified by the Authority.
	Cr Creditors	-	(2,617,089.00)	The Authority identified that the Children's Social Care accrual for services provided in 2023/24 where invoices had not been paid by year end was understated by £2,617k. The accrual of £4,173k processed was an estimate, and the underlying assumptions for the estimate were appropriate. The additional accrual was identified by the Authority after they carried out a piece of work on invoices paid in 2024/25 (from April 2024 to November 2024) to determine which year they related to. These totalled £6,790k.
	Dr Corporate Provisions Reserve	-	2,617,089.00	
	Cr MIRS	(2,617,089.00)	-	
Total		**£nil**	**£nil**	

We have also identified updates required to disclosures within the financial statements. Management made a manual presentational adjustment in the financial statements moving a debit to income into the expenditure column. This was reversed on request of the auditors and relates to £3,161k of prior year unidentified income drawn down from reserves.

DRAFT

Control Deficiencies

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

Priority rating for recommendations		
❶ **Priority one:** issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	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.	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.

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
1	②	**Management review of actuarial assumptions** Auditing standards define a management review control to include independent assessment of underlying assumptions by management. As part of our risk assessment procedures, we carried out a walkthrough to obtain an understanding of the pension assumption review process. We identified that there is no criteria or threshold developed for investigation/identification of outliers for pension assumptions. Therefore, although they do review the output of the actuary, there is no evidence of the review. Thus, there is not sufficiently well-defined process in place for it to meet the criteria of an effective review control. We recommend that management document the outcome of their annual review, including taking this to a relevant committee, to demonstrate appropriate challenge of the assumptions underlying the valuation. This should include demonstrating their view of their own assumptions to compare to those provided by the management expert.	TBC

DRAFT

Control Deficiencies

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
2	2	**Management review and challenge of valuation instructions and report** Our work over the PPE process did not identify a suitable control to be assessed as a management review control in line with the auditing standards. Whilst we understand that meetings were held with the Authority's valuers to discuss the scope of the valuation and a with WH&E, this process was not evidenced. We recommend that in the future, formal records are maintained and followed up with correspondence confirming the instructions. We also recommend that ahead of the next revaluation, a paper should be approved by Council or the appropriate Committee which covers the valuation approach. This can then feed into the instructions issued to the valuers and ensures that those charged with governance are aware of and satisfied with the approach.	TBC
3	2	**Overpayment of leavers** We identified one leaver form in a sample of 25 that was not submitted on a timely basis by the service department to payroll, resulting in a salary payment to the leaver after their leave date. We have confirmed that management are following up on debt collection for late leaver adjustments. We recommend that the process for notifying payroll of a leaver is reiterated to relevant service department staff, including recognition of timely notification.	TBC

DRAFT

Control Deficiencies

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
4	2	**Retention and maintenance of lease agreements** In a sample of 15 lease agreements selected for testing, nine of the agreements could not be located. Whilst alternative documentation was provided, the missing lease agreements could result in a risk if a dispute or disagreement over terms occurred. We also note that IFRS 16 lease disclosures are required for the Authority in 2024/25. Incomplete information about lease arrangements will make the disclosure more challenging to prepare in an accurate and complete manner. We recommend that management perform an exercise to understand the extent of missing lease arrangements, and, where material, consider the value of creating updated documentation. We also recommend that management review their policy for document retention of leases including where they should be stored, including a regular review of the information for completeness.	TBC
5	2	**IFRS 16 Pre-Implementation Disclosures** The Authority has not included complete IFRS 16 pre-transition disclosures in the draft financial statements Whilst they have included acknowledgement of the upcoming change in the standard, according to IAS 8, the disclosure should include a discussion of the estimated impact the introduction of new standards will have on the financial statements. If a reasonable estimate cannot be made due to data limitations, this fact should be disclosed. While the lack of quantitative disclosures in the 2023-24 financial statements is not considered an omission, given the standard's effective date of April 1, 2024, it is expected that management should be well advanced In their quantitative impact assessment for the 2024-25 financial statements. There is a risk that delaying this assessment could lead to errors, insufficient review time, and potentially material misstatements. Management should ensure that the quantitative impact assessment is schedules and completed promptly, allowing sufficient time for review and challenge before positing transition adjustments.	TBC

DRAFT

Control Deficiencies

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
6	2	**Related parties** The process performed by management to create the related parties disclosure in the financial statements does not include a step for assessing whether an interest declared by a relevant member does or does not meet the definition of a related party. The risk is over-disclosure of interests which are not related party transactions. We recommend that this step is introduced as part of the financial statements preparation process. We also recommend that the definition of related parties is regularly communicated to members to allow them to add more clarity to their declared interests to make this assessment possible.	TBC
7	3	**Staff costs amendments** We identified one amendment form in a sample of 25 which was not completed. This introduces a risk of error in amendments being made, and does not demonstrate appropriate authorisation of changes. We recommend that the Authority reiterates to all relevant employees the process for completing amendment forms, including in which situations this is likely to be needed. This could be through a form of training course.	TBC

DRAFT

Control Deficiencies

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date
8	3	**Reliance on specific individuals** Our audit procedures identified reliance on a small number of key individuals with sufficient knowledge to provide audit evidence to the team. This introduces a business continuity risk for the team with potential impact on operations if a key individual were to leave the Authority. We recommend the Authority revisits its business continuity procedures to confirm they are satisfied with the level of protection they are maintaining, including cover arrangements in the case of absence and appropriate documented process steps to be followed.	TBC
9	3	**PFI scheme monitoring of lifecycle replacement costs** During our testing of PFI contracts we identified a lack of record keeping of monitoring of PFI arrangements and difficulty by the Authority obtaining detailed information from PFI contractors about work completed, in respect of lifecycle replacement costs. We would expect management to understand the work being completed to ensure the Authority is receiving the services paid for and at the required standard. We understand that the Authority is introducing a review into PFI contracts which are expiring in the next 18 months including a full survey of works to be completed. We recommend that a monitoring control is introduced for other PFI arrangements to include documented checks of works completed being to the required standard for the Authority on a regular (annual) basis.	TBC

DRAFT

Control Deficiencies (cont.)

We have also follow up the recommendations from the previous years audit, in summary:

Total number of recommendations	Number of recommendations implemented	Number outstanding (repeated below):
4	4	0

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date	Current Status (November 2024)
1	2	There were still delays encountered in obtaining evidence to support samples selected for audit testing. This has an impact on the auditor's ability to complete the audit on a timely basis which has cost implications and increases the Council's audit fee. The Council need to continue to work on the capacity within the finance team. In addition, departments across the Council need to be reminded of the importance of providing documentation to support the audit to the finance team on a timely basis.	Core Accounting Recruitment and retention within the Core Finance team has been positive, with only one vacancy currently. There has also been the addition of an extra trainee accountant within the team. There was an all-finance closing of accounts session held on 01-Mar-24 which was well attended. At this it was made clear that areas of finance and services within the Council need to work with Core Accounting to respond to audit sample requests and queries. The Chief Accountant now attends the weekly management meetings with the Head of Service Finance and the Strategic Business Partners. At these meetings issues relating to closing are discussed. During the audit of the accounts these meetings will also be used to discuss, and chase responses to, audit queries.	Superseded by current year recommendations

DRAFT

Control Deficiencies (cont.)

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date	Current Status (November 2024)
2	2	Related Parties – One member had not returned their declaration of interest form. It was also identified that the process of recording gifts and hospitality needs strengthening. The current process is that Members submit one annual form with all the gifts and hospitality received in year. Members need to provide their annual declarations in time for preparation of the draft financial statements. Members need to disclose any offer of gift and hospitality as and when this is offered.	Committee Business Committee Business services have communicated with members the deadline for completing, signing and returning the declaration of interest form. This will be followed up to ensure a 100% return rate. The process of disclosing and recording gifts and hospitality is being reviewed.	Implemented
3	2	Testing of related party interests identified two Members that were directors in companies that had not disclosed these interests in their declaration form. The Members did not control either the Council or the companies so no disclosure in the financial statements was required. The Council need to undertake their own testing to ensure the completeness and accuracy of Members related party interest disclosures.	Core Accounting and Committee Business Guidance notes for Members on how to complete the interests in the declaration form are being revised to make it clear what a related party is, and how to identify one. When reviewing the declaration forms and compiling the backing for the Related parties note to the accounts officers will also carry out similar reviews that the auditors carry out. That is to search on Companies House for any companies that Members may be directors of.	Implemented

Control Deficiencies (cont.)

#	Risk	Issue, Impact and Recommendation	Management Response/Officer/Due Date	Current Status (November 2024)
4	2	The Council has significant credit balances on Council Tax and NNDR accounts due to residents and businesses. These balances have remained outstanding for several years. The Council need to take action to repay these creditors. In the instance where the residents or businesses cannot be traced and the legal time limits have expired, the Council should write back these amounts.	Resident and Business Services Action will take place during Summer to proactively contact customers where details are held to refund these sums. Where contact is not made, the amounts will be written off. Should customers contact Lewisham at any time, we will write back the credit and raise a refund All write off balances will be reported to the Director of Finance for review and approval. The project commenced in June-23 with more to follow during the year.	In progress Management update (Nov-23) The review has recently been completed for Business Rates accounts and £2m has been written back. The review of Council Tax accounts will be beginning shortly. Management update (June-24) The review of Council Tax is ongoing, currently the team are in the process of cleansing the data and the plan is to have the reviewed completed by 01 November 2024. Management update (Aug-24) For Business Rates accounts £3.3m has now been written back. For Council Tax a bespoke automation process has been developed and tested. £1.6m is due to be written back.

DRAFT

ISA (UK) 240 Revised: changes embedded in our practices

Ongoing impact of the revisions to ISA (UK) 240

ISA (UK) 240 (revised May 2021, effective for periods commencing on or after 15 December 2021) The auditor's responsibilities relating to fraud in an audit of financial statements included revisions introduced to clarify the auditor's obligations with respect to fraud and enhance the quality of audit work performed in this area. These changes are embedded into our practices and we will continue to maintain an increased focus on applying professional scepticism in our audit approach and to plan and perform the audit in a manner that is not biased towards obtaining evidence that may be corroborative, or towards excluding evidence that may be contradictory.

We will communicate, unless prohibited by law or regulation, with those charged with governance any matters related to fraud that are, in our judgment, relevant to their responsibilities. In doing so, we will consider the matters, if any, to communicate regarding management's process for identifying and responding to the risks of fraud in the entity and our assessment of the risks of material misstatement due to fraud.

Matters related to fraud that are, in our judgement, relevant to the responsibilities of Those Charged with Governance

Our assessment of the risks of material misstatement due to fraud may be found on page 5. We also considered the following matters required by ISA (UK) 240 (revised May 2021, effective for periods commencing on or after 15 December 2021) *The auditor's responsibilities relating to fraud in an audit of financial statements*, to communicate regarding management's process for identifying and responding to the risks of fraud in the entity and our assessment of the risks of material misstatement due to fraud:

- Concerns about the nature, extent and frequency of management's assessments of the controls in place to prevent and detect fraud and of the risk that the financial statements may be misstated.
- A failure by management to address appropriately the identified significant deficiencies in internal control, or to respond appropriately to an identified fraud.
- Our evaluation of the entity's control environment, including questions regarding the competence and integrity of management.
- Actions by management that may be indicative of fraudulent financial reporting, such as management's selection and application of accounting policies that may be indicative of management's effort to manage earnings in order to deceive financial statement users by influencing their perceptions as to the entity's performance and profitability.
- Concerns about the adequacy and completeness of the authorization of transactions that appear to be outside the normal course of business.

Based on our assessment, we have no matters to report to Those Charged with Governance.

DRAFT

ISA (UK) 315 Revised: changes embedded in our practices

Summary

In the prior period, ISA (UK) 315 Revised "Identifying and assessing the risks of material misstatement" was introduced and incorporated significant changes from the previous version of the ISA.

These were introduced to achieve a more rigorous risk identification and assessment process and thereby promote more specificity in the response to the identified risks. The revised ISA was effective for periods commencing on or after **15 December 2021**.

The revised standard expanded on concepts in the existing standards but also introduced new risk assessment process requirements – the changes had a significant impact on our audit methodology and therefore audit approach.

What impact did the revision have on audited entities?

With the changes in the environment, including financial reporting frameworks becoming more complex, technology being used to a greater extent and entities (and their governance structures) becoming more complicated, standard setters recognised that audits need to have a more robust and comprehensive risk identification and assessment mechanism.

The changes result in additional audit awareness and therefore clear and impactful communication to those charged with governance in relation to (i) promoting consistency in effective risk identification and assessment, (ii) modernising the standard by increasing the focus on IT, (iii) enhancing the standard's scalability through a principle based approach, and (iv) focusing auditor attention on exercising professional scepticism throughout risk assessment procedures.

Implementing year 1 findings into the subsequent audit plan

Entering the second year of the standard, the auditors will have demonstrated, and communicated their enhanced insight into their understanding of your wider control environment, notably within the area of IT.

In year 2 the audit team will apply their enhanced learning and insight into providing a targeted audit approach reflective of the specific scenarios of each entity's audit.

A key area of focus for the auditor will be understanding how the entity responded to the observations communicated to those charged with governance in the prior period.

Where an entity has responded to those observations a re-evaluation of the control environment will establish if the responses by entity management have been proportionate and successful in their implementation.

Where no response to the observations has been applied by entity, or the auditor deems the remediation has not been effective, the audit team will understand the context and respond with proportionate application of professional scepticism in planning and performance of the subsequent audit procedures.

What will this mean for our on-going audits?

To meet the on-going requirements of the standard, auditors will each year continue to focus on risk assessment process, including the detailed consideration of the IT environment.

Subsequent year auditor observations on whether entity actions to address any control observations are proportionate and have been successfully implemented will represent an on-going audit deliverable.

Each year the impact of the on-going standard on your audit will be dependent on a combination of prior period observations, changes in the entity control environment and developments during the period. This on-going focus is likely to result in the continuation of enhanced risk assessment procedures and appropriate involvement of technical specialists (particularly IT Audit professionals) in our audits which will, in turn, influence auditor remuneration.

DRAFT

KPMG's Audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.

To ensure that every engagement lead and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework. Responsibility for quality starts at the top through our governance structures as the UK Board is supported by the Audit Oversight Committee, and accountability is reinforced through the complete chain of command in all our teams.

Commitment to continuous improvement

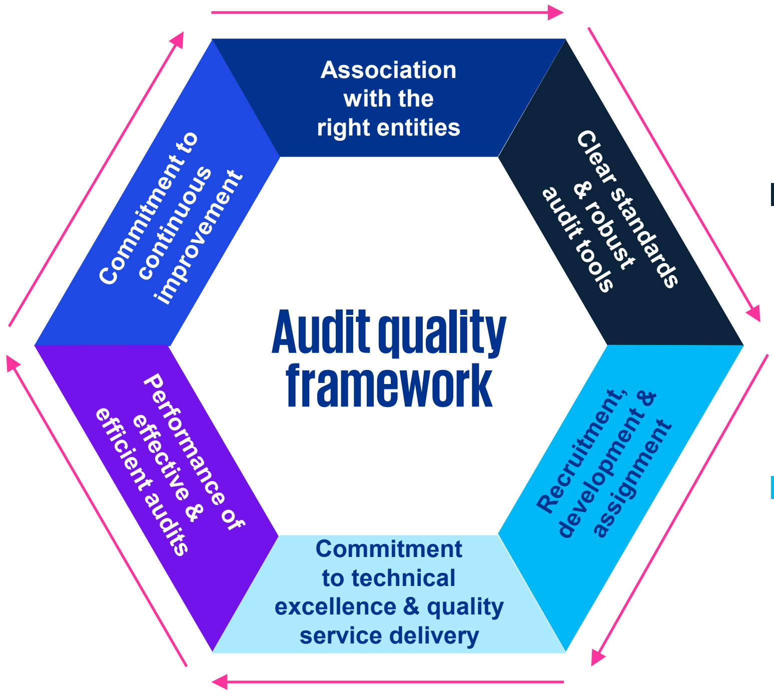
- Comprehensive effective monitoring processes
- Significant investment in technology to achieve consistency and enhance audits
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

Performance of effective & efficient audits

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching, including the second line of defence model
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Insightful, open and honest two way communications

Commitment to technical excellence & quality service delivery

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



Association with the right entities

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

Clear standards & robust audit tools

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- KPMG Clara incorporating monitoring capabilities at engagement level
- Independence policies

Recruitment, development & assignment of appropriately qualified personnel

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

kpmg.com/uk