

Audit Findings

Year ending 31 March 2018

West Mercia Energy
24 September 2018



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The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed for the purpose of expressing our opinion on the financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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Headlines

This table summarises the key issues arising from the audit of West Mercia Energy ('the Joint Committee') and the preparation of the Joint Committee's financial statements for the year ended 31 March 2018 for those charged with governance.

Financial Statements

Under the International Standards of Auditing (UK) (ISAs), we report whether, in our opinion:

- the Joint Committee's financial statements give a true and fair view of the Joint Committee's financial position and Joint Committee's expenditure and income for the year, and
- have been properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014.

We also report whether other information published together with the audited financial statements (including the Statement of Accounts, Annual Governance Statement (AGS) and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Our audit work was completed on site during July. Our findings are summarised on pages 4 to 9. We have not identified any adjustments to the financial statements that have resulted in an impact on the Statement of Comprehensive Income and Expenditure. Audit adjustments are detailed in Appendix B. We have also raised recommendations for management as a result of our audit work in Appendix A.

Subject to outstanding queries being resolved, we anticipate issuing an unqualified audit opinion following the Joint Committee meeting on 24 September 2018, and receipt of management representation letter

We have concluded that the other information published with the financial statements, which includes the Statement of Accounts, Annual Governance Statement and Narrative Report, are consistent our knowledge of your organisation and with the financial statements we have audited.

Acknowledgements

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

Summary

Overview of the scope of our audit

This Audit Findings presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management.

As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

Audit approach

Our audit approach was based on a thorough understanding of the Joint Committee's business and is risk based, and in particular included:

- An evaluation of the Joint Committee's internal controls environment including its IT systems and controls;
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks

Conclusion

We have substantially completed our audit of your financial statements and subject to outstanding queries being resolved, we anticipate issuing an unqualified audit opinion following the Joint Committee meeting on 24 September 2018.

Our approach to materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

Our assessment of the value of materiality has been adjusted on receipt of the 2017/18 draft accounts. We detail in the table below our assessment of materiality for West Mercia Energy.

	Joint Committee Amount (£)	Qualitative factors considered
Materiality for the financial statements	1,247k	2% of turnover <ul style="list-style-type: none"> • User expectation, prior year measures, entity concept of materiality, risk
Performance materiality	936k	75% of headline materiality <ul style="list-style-type: none"> • Experience of misstatement, business activities, accounting systems, people, controls, fraud risks
Trivial matters	62k	5% of headline materiality in line with ISAs
Materiality for specific transactions, balances or disclosures	50k	Remuneration disclosures <ul style="list-style-type: none"> • Materiality has been reduced due to sensitive nature and public interest in these disclosures

Going concern

Our responsibility

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK) 570).

Going concern commentary

Management's assessment process

Management have undertaken the following process in order to determine the applicability of the going concern assumption:

- Produced a detailed business plan for the 2018/19 period
- Obtained joint agreements between owning authorities
- Produced long term cash flow forecasts

Work performed

- Consideration of factors and events which may be indicative of a going concern issue or cast significant doubt over an entity's ability to continue as a going concern
- Review of management's supporting documents as stated above to understand whether assumptions used are reasonable
- Inquiries of key management personnel

Concluding comments

Auditor commentary

- Management have concluded that Joint Committee are a going concern and as such, the financial statements have been prepared on this basis.

Auditor commentary

- There are no factors that we are aware of which we consider would cast significant doubt over West Mercia Energy's ability to continue as a going concern
- Management assumptions in relation to cash flow, which is the key driver in ensuring solvency, appear reasonable
- The assessment provided extends to 12 months following the date of anticipated audit sign off accordingly.

Auditor commentary

- Overall, we are satisfied that the preparation of the financial statements using the going concern principal is reasonable
- The CIPFA Code negates the requirement to disclose the basis of preparation as this is assumed in public sector entities. No disclosure of material uncertainty is necessary for the Joint Committee
- Therefore, there will be no impact on our audit opinion related to going concern




Significant audit risks

Risks identified in our Audit Plan	Commentary
<p>1 Improper revenue recognition Under ISA 240 (UK) there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>For West Mercia Energy, we have concluded that the greatest risk of material misstatement relates to the occurrence of utility income</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> – review and testing of revenue recognition policies – performance of attribute testing on material revenue streams – review of unusual significant transactions <p>As a result of audit procedures performed, we have not identified any issues in relation to improper revenue recognition</p>
<p>2 Management override of controls Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities.</p> <p>We identified management override of controls as a risk requiring special audit consideration.</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> – review of accounting estimates, judgements and decisions made by management – testing of journal entries – review of unusual significant transactions <p>As a result of audit procedures performed, we have not identified any issues in relation to management override of controls. However, consistent with the prior period we have made a control recommendation in regards to senior financial reporting personnel's ability to post journal entries. More information is included at Appendix A.</p>
<p>3 Valuation of pension fund net liability The Joint Committee's pension fund asset and liability as reflected in its balance sheet represent a significant estimate in the financial statements.</p> <p>We identified the valuation of the pension fund net liability as a risk requiring special audit consideration</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> – Identified the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessed whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement – reviewed the competence, expertise and objectivity of the actuary who carried out the Joint Committee's pension fund valuation – gained an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made – confirmed the consistency of the pension fund net liability disclosures in notes to the financial statements with the actuarial report from your actuary <p>As a result of audit procedures performed, we have not identified any issues in relation to the valuation of the pension fund net liability</p>




Reasonably possible audit risks

Risks identified in our Audit Plan	Commentary
<p>1 Turnover – Utility revenue There is a risk in relation to the occurrence assertion that accounting for utility revenue is not consistent with the contracted terms</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> – documented our understanding of processes and key controls over the transaction cycle – Undertaken walkthroughs of the key controls to assess whether those controls were in line with our documented understanding and functioned effectively – Substantive attribute testing of a sample of utility revenue transactions included in the financial statements <p>As a result of audit procedures performed, we have not identified any issues in relation to the occurrence of utility revenue</p>
<p>2 Cost of goods sold – Utility expenditure There is a risk in relation to the valuation gross assertion that utility expenditure is not accounted for properly and is therefore understated</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> – documented our understanding of processes and key controls over the transaction cycle – Undertaken walkthroughs of the key controls to assess whether those controls were in line with our documented understanding and functioned effectively – Substantive attribute testing of a sample of utility expenditure transactions included in the financial statements <p>As a result of audit procedures performed, we have not identified any issues in relation to the accounting of utility expenditure</p>
<p>3 Cost of goods sold – Utility expenditure There is a risk in relation to the valuation net assertion that activity variations to utility expenditure contracts are not captured correctly and therefore adjustments are not processed accordingly</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> – documented our understanding of processes and key controls over the transaction cycle – Undertaken walkthroughs of the key controls to assess whether those controls were in line with our documented understanding and functioned effectively – review of contracts with supplier rebates and significant activity variation <p>As a result of audit procedures performed, we have not identified any issues in relation to the accounting of utility expenditure</p>

Accounting policies

Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	<ul style="list-style-type: none"> Revenue and capital transactions are accounted for on an accruals basis. This means that all revenue income is recorded when the debt has been established rather than when money has been received. 	<ul style="list-style-type: none"> The policy is appropriate under the relevant accounting framework, IFRS. Extent of judgement involved is low, and the range of possible outcomes and potential financial statement impact of different accounting policy choices would be minimal Disclosure of the accounting policy in the notes to the financial statements is adequate Accounting policy is reasonable when compared to peers and industry practice 	 Green
Judgements and estimates	<ul style="list-style-type: none"> Key estimates and judgements include: <ul style="list-style-type: none"> – Accruals – Valuation of pension fund net liability 	<ul style="list-style-type: none"> The accounting policies for areas of key estimate and judgement are adequately disclosed and appropriate under the relevant accounting framework, IFRS. Testing performed in relation to accruals has not identified any issues, we consider management procedures for calculation liabilities to be appropriate The extent of management judgment involved in the calculation of the net defined benefit obligation associated with the LGPS is minimal. Reliance is placed on actuarial experts of which we have corroborated and found to be reasonable 	 Green
Other critical policies		<ul style="list-style-type: none"> We have reviewed the Joint Committee's policies against the requirements of the CIPFA Code of Practice. The Joint Committee's accounting policies are appropriate and consistent with previous years. 	 Green

Assessment

-  Marginal accounting policy which could potentially be open to challenge by regulators
-  Accounting policy appropriate but scope for improved disclosure
-  Accounting policy appropriate and disclosures sufficient

Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

Issue	Commentary
① Matters in relation to fraud	<ul style="list-style-type: none"> We have previously discussed the risk of fraud with the Joint Committee. We have not been made aware of any incidents in the period and no other issues have been identified during the course of our audit procedures.
② Matters in relation to related parties	<ul style="list-style-type: none"> We are not aware of any related parties or related party transactions which have not been disclosed
③ Matters in relation to laws and regulations	<ul style="list-style-type: none"> You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
④ Written representations	<ul style="list-style-type: none"> A standard letter of representation has been requested from the Joint Committee, which is included in the Joint Committee papers.
⑤ Confirmation requests from third parties	<ul style="list-style-type: none"> We requested from management permission to send a confirmation request to NatWest bank. This permission was granted and the requests were sent and a positive confirmation was returned.
⑥ Disclosures	<ul style="list-style-type: none"> Our review found no material omissions in the financial statements.

Other responsibilities under the Code

Issue	Commentary
① Other information	<ul style="list-style-type: none"> We are required to give an opinion on whether the other information published together with the audited financial statements (including the Statement of Accounts, Annual Governance Statement (AGS) and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. <p>No inconsistencies have been identified. We plan to issue an unqualified opinion in this respect.</p>
② Matters on which we report by exception	<p>We are required to report on a number of matters by exception in a numbers of areas:</p> <ul style="list-style-type: none"> If the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the other information of which we are aware from our audit <p>We have nothing to report on this matters</p>

Independence and ethics

Independence and ethics

- We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Financial Reporting Council's Ethical Standard and confirm that we, as a firm, and each covered person, are independent and are able to express an objective opinion on the financial statements

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in December 2017 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.


Details of fees charged are detailed in Appendix C.

Audit and Non-audit services




No non-audit services have been provided to the Joint Committee.

Control recommendations

We have identified one recommendation for the Joint Committee as a result of issues identified during the course of our audit. We have agreed our recommendations with management and it should be noted. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

Assessment	Issue and risk	Recommendations
1	 <ul style="list-style-type: none"> Our review of the journals control environment has identified that the Director of the Joint Committee has the ability to post journal entries. We would not expect senior financial reporting personnel to have this level of access as it increases the risk of management override of controls. 	<p>We acknowledge that there are compensating controls in place to ensure all journals posted by the Director are reviewed and counter authorised by the Treasurer and that in practice no such postings have occurred in 2017/18</p> <p>However, we bring to the attention of those charged with governance this weakness in the control environment and recommend that journals access levels are reviewed to ensure only the appropriate individuals have the authority to prepare and post journal entries</p> <p>Management response</p> <p>In the absence of the Finance Manager, the Director would be required to process journals to allow the production of management accounts. All such transactions will continue to be authorised by the Treasurer of the Joint Committee. Every six months the Finance Manager will extract from the finance system a report detailing the journals posted over the six month period. This report will include reference to the person posting the journal and will be issued directly by the Finance Manager to the Treasurer</p>

Controls

-  High – Significant effect on control system
-  Medium – Effect on control system
-  Low – Best practice

Audit Adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Impact of adjusted/ unadjusted misstatements

As a result of audit procedures undertaken, we have not identified any misstatements for adjustment.

Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Disclosure omission	Detail	Adjusted?
Narrative Repot	<ul style="list-style-type: none">The requirements of the Narrative Report changed in 2017/18 and the Code now stipulates a number of areas this should cover. Our initial review of the Narrative Report identified that certain elements of the Code requirements had not been covered in detail	✓
Pensions	<ul style="list-style-type: none">Amendments were required to ensure mortality assumptions presented in the disclosure note to the financial statements agreed to the actuary report.	✓

Fees

We confirm below our final fees charged for the audit.

Audit Fees

	Proposed fee	Final fee
Joint Committee audit	£13,000	£13,000
Total audit fees (excluding VAT)	£13,000	£13,000



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