

Archwilydd Cyffredinol Cymru  
Auditor General for Wales



WALES AUDIT OFFICE  
SWYDDFA ARCHWILIO CYMRU

# Audit of Financial Statements Report

## **City & County of Swansea**

**Audit year:** 2015-16

**Issued:** September 2016

**Document reference:** 506A2016

# Status of report

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This document has been prepared as part of work performed in accordance with statutory functions.

In the event of receiving a request for information to which this document may be relevant, attention is drawn to the Code of Practice issued under section 45 of the Freedom of Information Act 2000. The section 45 Code sets out the practice in the handling of requests that is expected of public authorities, including consultation with relevant third parties. In relation to this document, the Auditor General for Wales and the Wales Audit Office are relevant third parties. Any enquiries regarding disclosure or re-use of this document should be sent to the Wales Audit Office at [info.officer@audit.wales](mailto:info.officer@audit.wales).

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The Auditor General intends to issue an unqualified audit report on the City & County of Swansea's financial statements, however there are some issues to report to you prior to their approval.

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# Summary report

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## Introduction

1. The Auditor General is responsible for providing an opinion on whether the financial statements give a true and fair view of the financial position of the City & County of Swansea (the Council) at 31 March 2016 and its income and expenditure for the year then ended.
2. We do not try to obtain absolute assurance that the financial statements are correctly stated, but adopt the concept of materiality. In planning and conducting the audit, we seek to identify material misstatements in your financial statements, namely, those that might result in a reader of the financial statements being misled.
3. The quantitative level at which we judge such misstatements to be material for the Council is £8.7 million. Whether an item is judged to be material can also be affected by certain qualitative issues such as legal and regulatory requirements and political sensitivity.
4. International Standard on Auditing (ISA) 260 requires us to report certain matters arising from the audit of the financial statements to those charged with governance of a body in sufficient time to enable appropriate action to be taken, should there be any required.
5. This report sets out for consideration the matters arising from the audit of the financial statements of the Council including the City & County of Swansea Group for 2015-16 which require reporting under ISA 260. A separate report has been issued for the City & County of Swansea Pension Fund.

## Status of the audit

6. We received the draft financial statements for the year ended 31 March 2016 a week before the deadline of 30 June 2016 and have now substantially completed our audit work. At the time of writing our audit was nearing completion but some areas of work remained outstanding.
7. Our Audit Plan for the Council issued in March 2016 sets out the audit risks which we considered to be significant. We have undertaken audit work to assess these risks and also considered any new risks which might have arisen. A summary of the audit risks, the audit work undertaken and our conclusions are shown in [Exhibit 1](#).

Exhibit 1: Audit risks, work undertaken and conclusion

Audit risk	Work undertaken and conclusion
<p><b>Risk of management override</b></p> <p>The risk of management override of controls is present in all organisations. Due to the unpredictable way in which such override could occur, it is viewed as a significant risk [ISA 240.31-33].</p>	<p>We have:</p> <ul style="list-style-type: none"> <li>• tested the appropriateness of journal entries and other adjustments made in preparing the financial statements;</li> <li>• reviewed accounting estimates for biases;</li> <li>• evaluated the rationale for any significant transactions outside the normal course of business; and</li> <li>• incorporated an element of ‘unpredictable audit work’, which varies each year.</li> </ul> <p>We have not identified any material issues although, as set out in <a href="#">Appendix 4</a>, we have concluded that the controls over journals need to be reviewed.</p>
<p><b>Risk of fraud in revenue recognition</b></p> <p>The level of income collected by the Council means that there is an inherent risk of material misstatement due to fraud in revenue recognition and as such is treated as a significant risk [ISA 240.26-27].</p>	<p>We have:</p> <ul style="list-style-type: none"> <li>• tested the appropriateness of a sample of journals processed to income and non-pay expenditure ledger codes during the year;</li> <li>• reviewed the application of relevant accounting policies to ensure that they are in compliance with accounting standards; and</li> <li>• analysed the various income streams and perform substantive procedures on a sample basis to ensure that income and has been appropriately accounted for in the correct period.</li> </ul> <p>We do not have any significant matters to report.</p>
<p><b>Risk of error with the valuation of property, plant and equipment (PPE) and investment properties</b></p> <p>The Council is required to ensure that for PPE and Investment Properties held on the balance sheet, the carrying amount is not materially different from the fair value of these assets at the year-end. This valuation process and the underlying assumptions adopted are subject to a number of judgements and changes in approach in 2015-16.</p>	<p>We have:</p> <ul style="list-style-type: none"> <li>• considered the appropriateness of the Council’s proposed approach to the valuation of PPE and Investment Properties; and</li> <li>• tested the valuation of such assets on a sample basis.</li> </ul> <p>The Council has made some progress with capital accounting arrangements during 2015-16 but, as set out below, further work is required in 2016-17.</p>

Audit risk	Work undertaken and conclusion
<p><b>Risk of provisions being materially misstated</b></p> <p>The Council's 2014-15 financial statements include a number of material provisions. These provisions will again be required in 2015-16 and, by their nature, they are uncertain and require a high degree of estimation. These include provisions for the future maintenance of land-fill sites and employee related expenses.</p>	<p>We have reviewed all material provisions to ensure that they are fairly stated. We do not have any significant matters to report.</p>
<p><b>Disclosure risks</b></p> <p>My audit team has held initial planning discussions with the Council which have identified a number of areas for further work including:</p> <ul style="list-style-type: none"> <li>• whether or not the Council is required to compile Group Accounts; and</li> <li>• what staff exit costs are disclosed in the financial statements.</li> </ul>	<p>We have discussed these issues with the Council and ensured disclosure requirements have been complied with.</p> <p>We do not have any significant matters to report although, as set out in <a href="#">Appendix 1</a>, we have made some disclosure amendments to the draft financial statements.</p>

8. We are now reporting to you the more significant issues arising from the audit, which we believe you must consider prior to approval of the financial statements. We have discussed these issues with Mike Hawes, the Director of Corporate Services.

## Proposed audit report

9. It is the Auditor General's intention to issue an unqualified audit report on the financial statements once you have provided us with a Letter of Representation based on that set out in [Appendix 1](#). The proposed audit report is set out in [Appendix 2](#).

## Significant issues arising from the audit

### Uncorrected misstatements

10. We identified one misstatement in the financial statements which we have discussed with management but which remains uncorrected. The misstatement and the reason for non-correction is set out in [Exhibit 2](#).

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## Exhibit 2: Uncorrected misstatements in the 2015-16 financial statements

Uncorrected misstatement	Reason for non-correction
<p>During 2015-16, the Council purchased carbon credits under the Carbon Reduction Scheme. This expenditure should have been treated as an intangible asset and a corresponding creditor established to offset the asset rather than the purchase just being charged to expenditure. In addition, at the year-end the Council has calculated that the carbon credits purchased are some £43,000 more than is required to settle the liability in October 2016. As a result:</p> <ul style="list-style-type: none"><li>• net assets were understated by £563,000;</li><li>• net liabilities were understated by £520,000; and</li><li>• net expenditure was overstated by £43,000.</li></ul>	<p>The amendment is not material and has only a marginal impact on the net expenditure, net reserves and net worth of the Council.</p>

## Corrected misstatements

11. There were a number of misstatements which have been corrected by management but which we consider should be drawn to your attention due to their relevance to your responsibilities over the financial reporting process. They are set out with explanations in [Appendix 3](#). These amendments had no impact on the net expenditure or net assets of the Council.

## Other significant issues arising from the audit

12. In the course of the audit, we consider a number of matters both qualitative and quantitative relating to the accounts and report any significant issues arising to you:
- **We have no significant concerns about the qualitative aspects of your accounting practices and financial reporting.** This is the first year of the audit for the Wales Audit Office and we found the financial statements were compiled to a good standard. We found the information provided to be relevant, reliable, comparable, material and easy to understand. We concluded that accounting policies and estimates are appropriate and financial statement disclosures unbiased, fair and clear. However, as set out below, further work is required to improve the Council's arrangements for accounting for fixed assets. We will hold a 'post project learning' meeting with the Finance Team later in the year to look at the financial statements compilation and audit processes. This meeting will also consider some of the challenges for next year such as the Highways Network Asset and earlier closure.
  - **We did not encounter any significant difficulties during the audit.** We generally received information in a timely and helpful manner and were not restricted in our work.
  - **There were no significant matters discussed and corresponded upon with management which we need to report to you.**

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- **There are no other matters significant to the oversight of the financial reporting process that we need to report to you.**
  - **We did not identify any material weaknesses in your internal controls although we have identified some significant issues to report to you.**  
**Appendix 4** set out our detailed findings and recommendations which are summarised as follows:
    - During 2015-16, the Council has made progress in improving its arrangements for capital accounting. This includes correctly revaluing Council Houses, revising its componentisation and indexation policies and reviewing its investment assets. However, there are a number of significant areas where further work is required in 2016-17 to ensure the correct treatment of non-enhancing capital expenditure, investment assets and council house land
    - Accountants currently have the facility to post and approve single journal entries up to a value of £250,000. Journal entries above £250,000 require manager approval. In our opinion this level is high and the Council should review its journal authorisation controls and limits and consider lowering the value at which journals require secondary approval.
    - The Council has a range of automated authorisation controls for its financial systems but some authorisation procedures are based on authorised signatories. A number of the authorised signatory lists we examined are out of date. Following the recent significant organisational restructure, the Council now needs to ensure its authorised signatory lists are up to date.
  - **There are no other matters specifically required by auditing standards to be communicated to those charged with governance.**

## Recommendations arising from our 2015-16 financial audit work

13. The key recommendations arising from our financial audit work are set out in **Appendix 4**. Management has responded to them and we will follow up progress on them during next year's audit. Where any actions are outstanding, we will continue to monitor progress and report it to you in next year's report.

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## Independence and objectivity

- 14.** As part of the finalisation process, we are required to provide you with representations concerning our independence. As reported in our Audit Outline there is one independence issue for which we put in place additional audit controls. We have complied with ethical standards and in our professional judgment, we are independent and our objectivity is not compromised.

# Appendix 1

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## Final Letter of Representation

Auditor General for Wales  
Wales Audit Office  
24 Cathedral Road  
Cardiff  
CF11 9LJ

## Representations regarding the 2015-16 financial statements

This letter is provided in connection with your audit of the financial statements of the City & County of Swansea (the Council) for the year ended 31 March 2016 for the purpose of expressing an opinion on their truth and fairness.

We confirm that to the best of our knowledge and belief, having made enquiries as we consider sufficient, we can make the following representations to you.

## Management representations

### Responsibilities

We have fulfilled our responsibilities for:

- The preparation of the financial statements in accordance with legislative requirements and the Code of Practice on Local Authority Accounting in the United Kingdom; in particular the financial statements give a true and fair view in accordance therewith.
- The design, implementation, maintenance and review of internal control to prevent and detect fraud and error.

### Information provided

We have provided you with:

- Full access to:
  - all information of which we are aware that is relevant to the preparation of the financial statements such as books of account and supporting documentation, minutes of meetings and other matters;
  - additional information that you have requested from us for the purpose of the audit; and
  - unrestricted access to staff from whom you determined it necessary to obtain audit evidence.

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- The results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
  - Our knowledge of fraud or suspected fraud that we are aware of and that affects the Council and involves:
    - management;
    - employees who have significant roles in internal control; or
    - others where the fraud could have a material effect on the financial statements.
  - Our knowledge of any allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, regulators or others.
  - Our knowledge of all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
  - We have informed you of any concerns raised or comments made by regulators about the pension fund, its fund managers and any assets/liabilities.
  - The identity of all related parties and all the related party relationships and transactions of which we are aware.

## Financial statement representations

All transactions, assets and liabilities have been recorded in the accounting records and are reflected in the financial statements.

Significant assumptions used in making accounting estimates, including those measured at fair value, are reasonable.

Related party relationships and transactions have been appropriately accounted for and disclosed.

All events occurring subsequent to the reporting date which require adjustment or disclosure have been adjusted for or disclosed.

All known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

The financial statements are free of material misstatements, including omissions. The effects of uncorrected misstatements identified during the audit are immaterial, both individually and in the aggregate, to the financial statements taken as a whole and we agree that they should remain uncorrected.

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## Representations by the City & County of Swansea

We acknowledge that the representations made by management, above, have been discussed with us.

We acknowledge our responsibility for the preparation of true and fair financial statements in accordance with the applicable financial reporting framework. The financial statements were approved by the Members of the City & County of Swansea on 22 September 2016.

We confirm that we have taken all the steps that we ought to have taken in order to make ourselves aware of any relevant audit information and to establish that it has been communicated to you. We confirm that, as far as we are aware, there is no relevant audit information of which you are unaware.

Director of Corporate Services

Chair of the Council

Date .....

Date .....

# Appendix 2

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## Auditor General for Wales' report to the Members of the City & County of Swansea

I have audited the accounting statements and related notes of:

- the City & County of Swansea;
- the City & County of Swansea Group; and
- the City & County of Swansea Pension Fund;

for the year ended 31 March 2016 under the Public Audit (Wales) Act 2004.

The City & County of Swansea's accounting statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Movement on the Housing Revenue Account Statement and the Housing Revenue Account Income and Expenditure Statement.

The City & County of Swansea Group's accounting statements comprise the Group Movement in Reserves Statement, the Group Comprehensive Income and Expenditure Statement, the Group Balance Sheet and the Group Cash Flow Statement.

The City & County of Swansea Pension Fund's accounting statements comprise the Fund Account and the Net Assets Statement.

The financial reporting framework that has been applied in their preparation is applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16 based on International Financial Reporting Standards (IFRSs).

### **Respective responsibilities of the responsible financial officer and the Auditor General for Wales**

As explained more fully in the Statement of Responsibilities for the Statement of Accounts set out on page 187, the responsible financial officer is responsible for the preparation of the statement of accounts, including the City & County of Swansea's Group accounting statements and the City & County of Swansea Pension Fund's accounting statements, which gives a true and fair view.

My responsibility is to audit the accounting statements and related notes in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Financial Reporting Council's Ethical Standards for Auditors.

### **Scope of the audit of the accounting statements**

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements and related notes sufficient to give reasonable assurance that the accounting statements and related notes are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the City & County of Swansea and the City & County of Swansea Group and the City & County of Swansea Pension Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the

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responsible financial officer and the overall presentation of the accounting statements and related notes.

In addition, I read all the financial and non-financial information in the Narrative Report to identify material inconsistencies with the audited accounting statements and related notes and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies, I consider the implications for my report.

### **Opinion on the accounting statements of the City & County of Swansea**

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of the City & County of Swansea as at 31 March 2016 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16.

### **Opinion on the accounting statements of the City & County of Swansea Group**

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of the City & County of Swansea Group as at 31 March 2016 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16.

### **Opinion on the accounting statements of the City & County of Swansea Pension Fund**

In my opinion, the pension fund accounts and related notes:

- give a true and fair view of the financial transactions of the City & County of Swansea Pension Fund during the year ended 31 March 2016 and of the amount and disposition of the fund's assets and liabilities as at that date; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16.

### **Opinion on other matters**

In my opinion, the information contained in the Narrative Report is consistent with the accounting statements and related notes.

### **Matters on which I report by exception**

I have nothing to report in respect of the following matters, which I report to you, if, in my opinion:

- adequate accounting records have not been kept;
- the accounting statements are not in agreement with the accounting records and returns; or
- I have not received all the information and explanations I require for my audit;

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- the Governance Statement does not reflect compliance with guidance.

**Certificate of completion of audit**

I certify that I have completed the audit of the accounts of the City & County of Swansea in accordance with the requirements of the Public Audit (Wales) Act 2004 and the Auditor General for Wales' Code of Audit Practice.

For and on behalf of  
Huw Vaughan Thomas  
Auditor General for Wales

Wales Audit Office  
24 Cathedral Road  
Cardiff  
CF11 9LJ

29 September 2016

# Appendix 3

## Summary of corrections made to the draft financial statements

During our audit we identified the following misstatements that have been corrected by management, but which we consider should be drawn to your attention due to their relevance to your responsibilities over the financial reporting process.

Value of correction	Nature of correction	Reason for correction
2015-16 £41,900,000 2014-15 £24,600,000	<b>Council House Capital Expenditure</b> The Council has written off non-enhancing Council House expenditure to the Capital Adjustment Account rather than the Revaluation Reserve. Although this is a technical accounting entry, it is not in accordance with the Code.  This amendment had an impact on all of the primary statements and several notes but the impact on net expenditure and net worth in both years is nil.  The draft financial statements were amended for this technical adjustment between unusable reserves.	To correct a material technical misstatement.
-	<b>Bad Debt Provision</b> The draft financial statements did not separately disclose the detail of the material bad debt provision.  Note 16 was amended to disclose the bad debt provision.	To include disclosure of the bad debt provision within the financial statements.
-	<b>Officers Remuneration over £60,000</b> The Council did not include severance and redundancy payments when calculating the remuneration bandings in Note 28. This is not in accordance with the Code.  Note 28 was amended to include all remuneration over £60,000, including severance and redundancy payments.  This increased the total number of officers disclosed from 64 to 78 in 2014-15 and from 69 to 86 in 2015-16.	To include disclosure of all officers receiving over £60,000 of total remuneration within the financial statements.

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Value of correction	Nature of correction	Reason for correction
-	<p><b>Post Balance Sheet Event</b></p> <p>A post balance sheet events note was not included in the draft financial statements. This is a disclosure requirement.</p> <p>A note was added to the draft financial statement to disclose that there were no post balance sheet events.</p>	<p>To include a disclosure note for post balance sheet events within the financial statements.</p>
-	<p>Various other minor presentational amendments were made to the draft financial statements.</p>	<p>To improve the readability of the financial statements.</p>

# Appendix 4

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## Recommendations arising from our 2015-16 financial audit work

We set out all the recommendations arising from our audit with management's response to them. We will follow up these next year and include any outstanding issues in next year's audit report.

### Matter arising 1 – Journal approval

<b>Findings</b>	Accountants have the facility to post and approve single journal entries up to a value of £250,000. Journal entries above £250,000 require manager approval.
<b>Priority</b>	Medium
<b>Recommendation</b>	The Authority should review its journal authorisation controls limits and consider lowering the value at which journals require secondary approval.
<b>Benefits of implementing the recommendation</b>	Implementation of the recommendation would improve the control environment by increasing the segregation of duties over journal processing.
<b>Accepted in full by management</b>	Yes
<b>Management response</b>	The Authority has restricted the processing of journals to Finance department staff to maintain control of the journals being processed in the General Ledger. The current limit ensures that all the material routine journals and technical year-end journals are approved by a manager. The Authority will review the journals posted in a financial year to try and reduce the number of journals processed by Finance staff. The Authority will review their journal approval limits to ensure they are at the appropriate limit for segregation of duty purposes and maintaining control. The Authority will need to consider the impact of reducing the journal approval limits on day to day operations.
<b>Implementation date</b>	2016-17

### Matter arising 2 – authorised signatory lists

<b>Findings</b>	The Council has a range of automated authorisation controls but some authorisation procedures are based on 'authorised signatory lists'. A number of the authorised signatory lists we examined are out of date.
<b>Priority</b>	Medium
<b>Recommendation</b>	Given there has been a significant recent restructure, the Council needs to ensure up to date signatory lists are in place across the Authority.

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### Matter arising 2 – authorised signatory lists

<b>Benefits of implementing the recommendation</b>	Implementation of the recommendation would improve the control environment by improving authorisation controls.
<b>Accepted in full by management</b>	Yes
<b>Management response</b>	<p>Whilst this is an important issue, the reality is that a significant number of authorisations are now undertaken electronically by workflow within the Councils ORACLE systems and, as such, manual authorisation lists become less important.</p> <p>It is essential however that the Council can evidence authorisation limits and we will work to get clarity around this.</p>
<b>Implementation date</b>	2016-17

### Matter arising 3 – accounting for capital

<b>Findings</b>	<p>During 2015-16 the Council has made some progress in improving its arrangements for capital accounting. This includes correctly revaluing Council Houses, revising its componentisation and indexation policies and reviewing its investment assets. However, there are a number of areas where further work is required in 2016-17 including:</p> <ul style="list-style-type: none"><li>• The Council's current approach for the treatment of non-enhancing capital expenditure is not fully compliant with CIPFA's Code. Further work will be required to ensure that the Council has a clear policy for non-enhancing expenditure and that this is complied with.</li><li>• The Council needs to review its policy for investment assets and, following this, determine whether assets currently held as investments assets are correctly categorised.</li><li>• The Council needs to re-examine its Council House valuation to identify a land value. The Council then needs to ensure that land is not depreciated.</li><li>• The Council's asset register is spreadsheet based which takes significant officer time to maintain. The Council should look at a more efficient solution.</li></ul>
<b>Priority</b>	High
<b>Recommendation</b>	The Council needs to continue to improve its capital accounting arrangements in 2016-17 across a number of areas.
<b>Benefits of implementing the recommendation</b>	Implementation of the recommendation would improve capital accounting arrangements.
<b>Accepted in full by management</b>	Yes

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### Matter arising 3 – accounting for capital

#### Management response

The method adopted by the Council for accounting for non-enhancing Capital expenditure has been unchanged over a number of years and was adopted with the full approval of the Council's previous operational Auditors, PwC LLP.

However, as these adjustments have no effect on the financial standing or financial performance of the Council, we will adopt them as a matter of course.

The accounting treatment of non-enhancing capital expenditure will be reviewed and the relevant changes implemented. All investment properties will be reviewed to ensure that they are in the appropriate asset category. The Authority will work with the auditors to ensure that there is an appropriate land value for council dwelling assets. By working with the auditors the Authority is hoping to simplify capital accounting so that we can automate processes and reduce the manual workload.

#### Implementation date

2016-17



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