

Annual Audit Letter

West Yorkshire Combined Authority



For the year ended 31 March 2017



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Executive summary

Purpose of this report

Our Annual Audit Letter summarises the work we have undertaken as the auditor for West Yorkshire Combined Authority ('the Combined Authority'] for the year ended 31 March 2017. Although this letter is addressed to the Combined Authority, it is designed to be read by a wider audience including members of the public and other external stakeholders.

Our responsibilities are defined by the Local Audit and Accountability Act 2014 ('the 2014 Act') and the Code of Audit Practice issued by the National Audit Office ('the NAO'). The detailed sections of this letter provide details on those responsibilities, the work we have done to discharge them, and the key findings arising from our work. These are summarised below.

Area of work	Summary
Financial statements opinion	<p>On 29 August 2017 we issued our opinion that:</p> <ul style="list-style-type: none">the financial statements give a true and fair view of the Combined Authority's financial position as at 31 March 2017 and of its financial performance for the year then ended.
Opinions on other matters	<p>On 29 August 2017 we issued our opinion that:</p> <ul style="list-style-type: none">the Narrative Report published with the financial statements, is consistent with those financial statements.
Value for Money conclusion	<p>On 29 August 2017 we issued our conclusion that the Combined Authority had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources.</p>
Whole of Government Accounts	<p>In line with instructions issued by the NAO, on 28 September 2017 we issued our assurance certificate which reported that the Council's consolidation pack was consistent with the audited financial statements.</p>
Matters that we report by exception	<p>We have not identified any matters to report in relation to:</p> <ul style="list-style-type: none">whether the Annual Governance Statement is in line with our understanding of the Combined Authority and the requirements of the Delivering Good Governance in Local Government Framework 2016;reports in the public interest or written recommendations made under s24 of the 2014 Act;exercise of other audit powers under the 2014 Act.

As we have discharged all of our responsibilities under the 2014 Act for the 2016/17 audit, we certified the closure of the audit on 28 September 2017.

Audit of the financial statements

Financial statements opinion

Unqualified

The scope of our audit and the results of our work

The purpose of our audit is to provide reasonable assurance to users that the financial statements are free from material error. We do this by expressing an opinion on whether the statements are prepared, in all material respects, in line with the financial reporting framework applicable to the Combined Authority and whether they give a true and fair view of the Combined Authority's financial position as at 31 March 2017 and of its financial performance for the year then ended.

Our audit was conducted in accordance with the requirements of the Code of Audit Practice issued by the NAO, and International Standards on Auditing for the UK and Ireland (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the Combined Authority's circumstances and have been consistently applied and adequately disclosed;
- the significant accounting estimates made by management in the preparation of the financial statements are reasonable; and
- the overall presentation of the financial statements provides a true and fair view.

Our approach to materiality

We apply the concept of materiality when planning and performing our audit, and when evaluating the effect of misstatements identified as part of our work. We consider the concept of materiality at numerous stages throughout the audit process, in particular when determining the nature, timing and extent of our audit procedures, and when evaluating the effect of uncorrected misstatements. An item is considered material if its misstatement or omission could reasonably be expected to influence the economic decisions of users of the financial statements.

Judgements about materiality are made in the light of surrounding circumstances and are affected by both qualitative and quantitative factors. As a result we have set materiality for the financial statements as a whole (financial statement materiality) and a lower level of materiality for specific items of account (specific materiality) due to the nature of these items or because they attract public interest. We also set a threshold for reporting identified misstatements to the Governance and Audit Committee. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 March 2017:

Financial statement materiality	£5.354 million
Specific materiality	We have applied a lower level of materiality to the following items of account: <ul style="list-style-type: none">• Senior officer remuneration• Members' allowances• Exit packages
Trivial threshold	£0.161 million

Our response to significant risks

As part of our continuous planning procedures we considered whether there were risks of material misstatement in the Combined Authority's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Governance and Audit Committee within our Audit Strategy Memorandum and provided details of how we responded to those risks in our Audit Completion Report. The table below outlines the identified significant risks, the work we carried out on those risks and our conclusions.

Significant risk	How we addressed the risk	Audit conclusion
<p>Management override of control</p> <p>In all entities, management at various levels within an organization are 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. Due to the unpredictable way in which such overrides could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.</p>	<p>We addressed this risk by:</p> <ul style="list-style-type: none"> • using a computer audit analytical technique to identify journals with specific risk characteristics and testing the basis for such adjustments; • evaluating and testing the basis for material accounting estimates, which may be subject to management bias, included in the financial statements; and • reviewing unusual or significant transactions outside the normal course of business. 	<p>Our work provided the assurance we sought and did not highlight any material issues to bring to your attention. There is no indication of management override of controls.</p>
<p>Revenue Recognition</p> <p>In accordance with international standards on auditing (ISA 240) we presume there is a risk of fraud in respect of the recognition of revenue because of the potential for inappropriate recording of transactions in the wrong period. We identified the following as key areas of focus for the significant risk:</p> <ul style="list-style-type: none"> • grant income is recognised when all conditions attached to the grant have been met so there is significant management judgement in determining when the conditions have been met; and • prepaid ticket income is recognised based on sale information from a variety of sources including travel centres, railway stations and payzone. 	<p>We evaluated the design and implementation of controls to mitigate the risk of income being recognised in the wrong period. In addition, we will undertake a range of substantive procedures including:</p> <ul style="list-style-type: none"> • testing receipts in March and April to June 2017 to ensure they have been recognised in the right year; • reviewing the reasonableness of the judgements made by management in determining whether grant conditions have been met; and • testing the recognition of prepaid ticket income to information and returns from sales outlets to ensure income has been recognised in the right year. 	<p>Our audit work provided the assurance we sought and did not identify any material issues to bring to your attention. We found no indication of revenue being recognised in the wrong year.</p>

<p>Pension estimation (IAS19)</p> <p>The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.</p>	<p>We discussed with key contacts any significant changes to the pension estimates prior to the preparation of the financial statements. In addition to our standard programme of work in this area, we:</p> <ul style="list-style-type: none"> evaluated the management controls you have in place to assess the reasonableness of the figures provided by the actuary; and considered the reasonableness of the actuary's output, referring to an expert's report on all actuaries nationally which is commissioned annually by the National Audit Office. 	<p>Our audit work provided the assurance we sought and did not identify any material issues to bring to your attention. We found no indication of material estimation error in respect of pensions.</p>
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Internal control recommendations

As part of our audit we considered the internal controls in place that are relevant to the preparation of the financial statements. We did this to design audit procedures that allow us to express our opinion on the financial statements, but this did not extend to us expressing an opinion on the effectiveness of internal controls. We identified the following deficiencies in internal control as part of our audit.

Description of deficiency	We write to third parties to obtain confirmation of loans made by the Combined Authority. We received a response from another local authority that they do not recognise a loan of £300,000 made from Local Growth Fund in February 2016 and consider that it is a grant. Management have provided us with evidence of a loan agreement signed by the counterparty.
Potential effects	There is a risk that the counterparty might dispute the repayment of the loan.
Recommendation	The Combined Authority should ensure that the status of this loan is resolved with the counterparty.
Management response	Agreed. The status of the loan will be resolved with the counterparty as soon as possible.

Value for Money conclusion

Value for Money conclusion

Unqualified

Summary of our work

We are required to form a conclusion as to whether the Combined Authority made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out in order to form our conclusion, and sets out the criterion and sub-criteria that we are required to consider.

The overall criterion is that, 'in all significant respects, the Combined Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.' To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:

- informed decision making;
- sustainable resource deployment; and
- working with partners and other third parties.

The following table provides commentary of our findings in respect of each of the sub-criteria and an indication as to whether proper arrangements are in place.

Sub-criteria	Commentary	Arrangements in place?
Informed decision making	<p>The Combined Authority has a clear governance structure which is described on its website and includes the expected features of an effective governance framework within local government.</p> <p>During the year the Combined Authority embarked on its 'One Organisation' Programme designed to put in place the right structures, processes and people to deliver the Authority's objectives and priorities.</p> <p>The Corporate Plan sets out the Combined Authority's priorities and is closely aligned to the overarching aims of the Strategic Economic Plan. The Corporate Plan is supported by revenue and capital budgets.</p> <p>The Medium Term Financial Strategy which is reviewed and refreshed annually reflects strategic objectives and allocates resources to priority areas. In addition, regular financial reporting takes place through the Organisational Management Team and Leadership Team, with regular reporting to the Combined Authority.</p>	Yes

	<p>LEP panels are being incorporated within the Authority's decision-making structure improving transparency and accountability.</p> <p>There is a Risk Manual which sets out the risk management strategy and the way risks are identified, recorded and monitored. Management have agreed to implement Internal Audit recommendations to strengthen risk management arrangements.</p> <p>During the year the project management framework has been refined establishing a Portfolio Management Office with a well-defined three-stage project approval process. Partner bodies delivering projects funded by the Combined Authority are required to follow this framework.</p> <p>The system of internal control is subject to Internal Audit and for 2016/17, the Combined Authority's internal auditors, provided an opinion of reasonable assurance.</p> <p>A Governance and Audit Committee is in place to oversee the governance framework including the work of internal audit and approval of the Combined Authority's financial statements. Arrangements are being strengthened by recruitment of an independent member of the Governance and Audit Committee.</p>	
Sustainable resource deployment	<p>The Combined Authority has made good progress in addressing the financial challenges from public sector austerity and has a proven track record of strong budget management and delivering planned budget reductions.</p> <p>The Combined Authority delivered financial outturn for 2016/17 £1.4 million better than originally planned which was consistent with recent financial reporting. This reflects additional operational savings including £1 million on concessionary travel expenditure.</p> <p>A balanced budget has been set for 2017/18 with use of £2.3 million of reserves consistent with the three year Medium Term Financial Strategy covering the years 2017/18 to 2019/20.</p> <p>The Combined Authority has also recognised the significant financial challenge facing the districts and has agreed to reductions in the transport levy.</p> <p>The capital programme reflects priorities set out in the Corporate Plan flowing from the Strategic Economic Plan.</p>	Yes
Working with partners and other third parties	<p>The Combined Authority has refreshed the Strategic Economic Plan for Leeds City Region as a framework for engagement with others within the City Region and beyond across private, public and third sectors to deliver good growth.</p> <p>The Combined Authority is an active participant in sub-regional networks and leads on 'Transport for the North' work-streams on 'Local Strategic Connectivity' and 'Integrated and Smart Travel'.</p> <p>It responds to consultations, for example on the Government's green paper on industrial strategy and consultation on the Northern Powerhouse Strategy.</p> <p>Procurement arrangements are in place to secure cost effective purchasing.</p>	Yes

Significant Value for Money risks

The NAO's guidance requires us to carry out work to identify whether or not a risk to the Value for Money conclusion exists. Risk, in the context of our work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Combined Authority being inadequate. In our Audit Strategy Memorandum, we reported that for 2016/17, we had not identified any significant risks for our VFM conclusion. We did, however, identify areas of additional work. The additional work we carried out is outlined below.

Area of additional work	Work undertaken	Conclusion
<p>Sustainable resource deployment</p> <p>Last year we assessed the Combined Authority's arrangements for medium term financial planning as robust. We are not aware of any matters to suggest a significant change in arrangements.</p> <p>The Combined Authority continues to face financial pressure in the coming years including a reduction in the transport levy by £1m for 2017/18 and potentially by £2m for 2018/19 to 2019/20. A reduction of £1m equates to a 2% saving requirement in discretionary expenditure.</p> <p>We need to ensure our knowledge of financial planning arrangements and monitoring of the planned delivery of savings, remains up to date in order to ensure we give the correct VFM conclusion.</p>	<p>Building on our existing understanding, our work included reviewing:</p> <ul style="list-style-type: none"> • how the Combined Authority has developed its medium term financial strategy; • the delivery of 2016/17 savings against plans; • the arrangements for 2017/18 savings, including review of robustness of identified plans; and • the arrangements for identifying savings in 2018/19 to 2019/20. 	<p>We identified no matters to suggest a significant value for money audit risk.</p>

Other reporting responsibilities

Exercise of statutory reporting powers	No matters to report
Annual Governance Statement	No matters to report
Whole of Government Accounts consistency with the financial statements	Consistent
Other information published alongside the financial statements	Consistent

The NAO's Code of Audit Practice and the 2014 Act place wider reporting responsibilities on us, as the Combined Authority's external auditor. We set out below, the context of these reporting responsibilities and our findings for each.

Matters which we report by exception

The 2014 Act provides us with specific reporting powers where matters come to our attention that require reporting to parties other than the Combined Authority. We have the power to:

- report in the public interest; and
- make statutory recommendations to the Combined Authority, which must be responded to publicly.

In addition we must respond to any objections or questions on items contained within the accounts raised by a local government elector. We did not receive any such objections or questions.

We are also required to report if, in our opinion, the Annual Governance Statement does not comply with the guidance issued by CIPFA in 'Delivering Good Governance in Local Government; Framework 2016' or is inconsistent with our knowledge and understanding of the Combined Authority.

We did not exercise any of our reporting powers during our 2016/17 audit and had no matters to report to the Combined Authority in relation to the Annual Governance Statement.

Reporting to the NAO in respect of Whole of Government Accounts

The NAO requires us to report to them whether consolidation data that the Combined Authority has submitted is consistent with the audited financial statements, and to undertake specified procedures on that data. We have concluded and reported that the consolidation data is consistent with the audited financial statements.

Other information published alongside the financial statements

The Code of Audit Practice requires us to consider whether information published alongside the financial statements is consistent with those statements and our knowledge and understanding of the Combined Authority. In our opinion, the information in the Narrative Report is consistent with the audited financial statements.

Our fees

Fees for work as the Combined Authority's appointed auditor

We reported our proposed fees for our audit work in our Audit Strategy Memorandum presented to the Governance and Audit Committee in April 2017. We confirm that these fees are in line with the scale fee set by Public Sector Audit Appointments.

Having completed our work for the 2016/17 financial year, we can confirm that our final fees are as follows:

Area of work	2016/17 proposed fee	2016/17 final fee
Core audit work required by the NAO's Code of Audit Practice	£33,720	£33,720
Other non-Code work	£2,000	£2,000

Non-Code work relates to assurance work certifying grants for which fees were agreed separately with officers.

Future challenges

Financial outlook

The Combined Authority has made good progress in addressing its challenges to date and has a proven track record of budget management and delivering planned budget reductions. In common with most authorities, the Combined Authority faces a continuing financial challenge to maintain services at a time of unprecedented reductions in local government funding.

The revenue funding for many of the Combined Authority's activities comes mainly from the transport levy (£95 million) on West Yorkshire local authorities, with further contributions from them and the other City Region authorities for economic activities. The financial pressures facing these authorities will continue to impact on future levy levels. The Combined Authority's scope for savings is constrained by the high proportion of non-discretionary expenditure such as £43 million from the transport levy spent on the statutory English National Concessionary Scheme.

The budget for 2017/18 includes funding from government and other agencies for business and skills activities although much of the funding is non-recurrent and is currently expected to reduce significantly for 2018/19 unless further funds can be secured. Overall the Combined Authority faces a funding gap of £4 million as it develops its budget for 2018/19 and there is little scope to use reserves to close this gap. The Combined Authority is working hard on a range of options to make further savings and improve efficiency.

Operational challenges

The Combined Authority's workload has been increasing due in part to the Growth Deal funding which requires greater delivery capacity and additional support from policy and other teams. The Combined Authority is continuing to implement its 'One Organisation' initiative to streamline its approach and to ensure closer alignment between strategy, policy and delivery.