External Audit Plan

Year ending 31 March 2018

Merseyside Waste Disposal Authority

20 February 2018

Appendix 1

7

Contents

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The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit planning process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect the Authority or any weaknesses in your internal controls. 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.

Introduction & headlines

Purpose

This document provides an overview of the planned scope and timing of the statutory audit of Merseyside Waste Disposal Authority ('the Authority') for those charged with governance.

Respective responsibilities

The National Audit Office ('the NAO') has issued a document entitled Code of Audit Practice ('the Code'). This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. Our respective responsibilities are also set in the Terms of Appointment and Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA), the body responsible for appointing us as auditor of Merseyside Waste Disposal Authority. We draw your attention to both of these documents on the PSAA website.

Scope of our audit

The scope of our audit is set in accordance with the Code and International Standards on Auditing (ISAs) (UK). We are responsible for forming and expressing an opinion on the:

- financial statements (including the Annual Governance Statement) that have been prepared by management with the oversight of those charged with governance (the Authority); and
- Value for Money arrangements in place at the Authority for securing economy, efficiency and effectiveness in your use of resources.

The audit of the financial statements does not relieve management or the Authority of your responsibilities. It is the responsibility of the Authority to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Authority is fulfilling these responsibilities.

Our audit approach is based on a thorough understanding of the Authority's business and is risk based.

Introduction & headlines

Significant risks	Those risks requiring specific audit consideration and procedures to address the likelihood of a material financial statement error have been identified as: • Management override of control • Accounting for changes in the Authority's operations resulting from the Resource Recovery Contract (RRC). We will communicate significant findings on these areas as well as any other significant matters arising from the audit to you in our Audit Findings (ISA 260) Report.
Materiality	We have determined planning materiality to be £1.299m, which equates to 1.7% of your 2016/17 gross cost of services expenditure (£1.295m for Group Accounts). Our prior year materiality was £1.299m based on the same 1.7% benchmark (£1.294 for Group Accounts). We are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. Clearly trivial has been set at £0.065m (2016/17 £0.065m). ISA (UK and Ireland) 320 also requires auditors to determine lower materiality levels where there are "particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users". We have identified the following disclosure where a lower materiality level is appropriate: Disclosures of senior manager salaries and allowances in the remuneration report – Due to public interest in these disclosures and the statutory requirement for them to be made, we have set a materiality level of £20,000.
Value for Money arrangements	Our initial risk assessment regarding your arrangements to secure value for money has identified the following VFM significant risks: • the Authority continues to face on-going financial pressures but has continued to manage its finances to deliver a balanced outturn position. However, to avoid levy increases over a number of years, continued use has been made of the Authority's reserves to achieve a balanced budget. This has resulted in general reserves falling to £11.64 million at the end of 2016/17. The planned use of general reserves during 2017/18 is expected to reduce the Authority's available reserves to £2.47m at 31 March 2018 • the Resource Recovery Contract (RRC) became operational on 1 September 2017. Given the significant size of the RRC and the operational impact on the Authority, there is a need for the Authority to ensure effective governance arrangements are in place to manage the contract, including contract variations, review key targets and outputs, monitor budgets and their achievement, as well as ensure effective reporting.
Audit logistics	Our interim visit will take place in February and our final visit will take place in June and July 2018. Our key deliverables are this Audit Plan and our Audit Findings Report. PSAA's indicative fee for the Authority for 2017/18 is £29,363 (2016/17: £29,363). We have agreed to keep the Director of Finance updated on any fee implications arising from additional work in connection with the Resource Recovery contract.
Independence	We have complied with 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.

Deep business understanding

Changes to service delivery

Resource Recovery Contract

The Authority awarded a 30-year contract valued at over £1 billion to Sita Sembcorp UK (SSUK) in December 2013.

The contract will see waste transported from the region to a new energy from waste facility and will deliver significant savings to the Authority's partner Councils. The new facility in the North East of England became operational on 1 September 2017 and will be accounted for in the Authority’s financial statements from 2017/18.

Changes to financial reporting requirements

Accounts and Audit Regulations 2015 (the Regulations)

The Department of Communities and Local Government (DCLG) is currently undertaking a review of the Regulations, which may be subject to change. The date for any proposed changes has yet to be confirmed, so it is not yet clear or whether they will apply to the 2017/18 financial statements.

Accounts Publication

Under the 2015 Regulations, local authorities and other local government bodies are required to publish their accounts along with the auditors opinion by 31 July 2018.

Changes to the CIPFA 2017/18 Accounting Code

CIPFA have introduced other minor changes to the 2017/18 Code which confirm the going concern basis for local authorities, and updates on Leases, Service Concession arrangements and financial instruments.

Key challenges

Financial position

The Authority’s 2017/18 budget shows expenditure of £75.3 million. The latest 2017/18 outturn report indicates a small £356K overspend against budget at the year end.

The Authority’s reserves have continued to be used over the last few years to avoid levy increases reducing general reserves. At the end of 2016/17, general reserves totalled £11.64 million and by 31 March 2018 are expected to fall to £2.47 million. If reserves are utilised as planned during the year, the Authority’s General reserves will almost be depleted at the year end limiting the Authority’s ability to deal with any significant unforeseen events.

We understand that at the Authority meeting on 3 February 2018, agreement was reached for a levy increase of 9% in 2018/19. In addition, an indicative 7% increase in 2019/20 and 2.8% in 2020/21 was discussed.

Our response

- As part of our opinion on your financial statements, we will consider whether your financial statements accurately reflect the accounting entries and disclosures for the Resource Recovery Contract.
- We will consider your arrangements for managing and reporting your financial resources and your progress against planned service delivery changes, as part of our work in reaching our Value for Money conclusion.
- We will keep you informed of changes to the Accounts and Audit Regulations and any associated changes to financial reporting or public inspection requirements for 2017/18 through on-going discussions and invitations to our technical update workshops.

Significant risks identified

Significant risks are defined by professional standards as risks that, in the judgement of the auditor, require special audit consideration because they have a higher risk of material misstatement. Such risks often relate to significant non-routine transactions and judgmental matters. In identifying risks, audit teams consider the nature of the risk, the potential magnitude of misstatement, and its likelihood.

Risk	Reason for risk identification	Key aspects of our proposed response to the risk
The revenue cycle includes fraudulent transactions	Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.	Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Authority, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: • there is little incentive to manipulate revenue recognition • opportunities to manipulate revenue recognition are very limited • the culture and ethical frameworks of local authorities, including MWDA, mean that all forms of fraud are seen as unacceptable. Therefore, we do not consider this to be a significant risk for MWDA.
Management over-ride 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. Management over-ride of controls is a risk requiring special audit consideration.	We will: • gain an understanding of the accounting estimates, judgements applied and decisions made by management and consider their reasonableness • obtain a full listing of journal entries, identify and test unusual journal entries for appropriateness • evaluate the rationale for any changes in accounting policies or significant unusual transactions.

Significant risks identified

Risk	Reason for risk identification	Key aspects of our proposed response to the risk
Accounting for changes in the Authority's operations	The Resource Recovery Contract, a Public Private Partnership (PPP) scheme became fully operational on 1 September 2017. The risk is that the new asset recognised under this scheme is that fair value is not materially misstated as at 1 September 2017 and that any impairment of bringing this asset into use as at this date has been correctly calculated. The Authority will fully account for its contractual arrangement with Sita Sembcorp UK in its 2017/18 financial statements and in future years. Given the significant size of the contract and the complex nature of the accounting requirements, we have identified the accounting model to be used, the associated accounting entries and disclosures to be made in the financial statements as a risk requiring special consideration in this first year.	We will: • Examine and test the accuracy of the accounting entries and disclosures proposed. ▪ We plan to review the review management's processes and assumptions for the calculation of the value of the RRC, the instructions issued to valuation experts and the scope of their work ▪ consider the competence, specialist expertise and objectivity of the valuer, especially given the specialised nature of the assets under this scheme. ▪ discuss with the valuer the basis on which the valuation is carried out and examine the key assumptions • Gain an understanding of the changed operations and accounting position proposed in discussion with management and the Authority's consultant (Peter Worth) • Review the accounting model developed and the entries proposed for reasonableness against our understanding of the RRC. • Review whether impairments have been identified in accordance with IAS36.

We will communicate significant findings on these areas as well as any other significant matters arising from the audit to you in our Audit Findings Report in July 2018.

Reasonably possible risks identified

Reasonably possible risks (RPRs) are, in the auditor's judgment, other risk areas which the auditor has identified as an area where the likelihood of material misstatement cannot be reduced to remote, without the need for gaining an understanding of the associated control environment, along with the performance of an appropriate level of substantive work. The risk of misstatement for an RPR is lower than that for a significant risk, and they are not considered to be areas that are highly judgmental, or unusual in relation to the day to day activities of the business.

Risk	Reason for risk identification	Key aspects of our proposed response to the risk
Operating expenses	Non-pay expenses on other goods and services (including contract payments) represents a significant percentage of the Authority's operating expenses. Management uses judgement to estimate accruals of un-invoiced costs. We have identified completeness of non-pay expenses as a risk requiring particular audit attention.	We will • evaluate the Authority's accounting policy for recognition of non-pay expenditure for appropriateness • gain an understanding of the Authority's system for accounting for non-pay expenditure and evaluate the design of the associated controls • undertake expenditure cut-off testing • complete substantive testing of a sample of year end creditor balances.

Reasonably possible risks-continued

Risk	Reason for risk identification	Key aspects of our proposed response to the risk
Valuation of property, plant and equipment	The Authority completed a revaluation of its asset base on 31/3/16. This valuation will inform the basis of valuation of assets recorded in the 2017-18 financial statements after taking into account any impairments, fixed asset additions and disposals and any other circumstances that have significantly affected the valuation of assets since this last revaluation. This represents a significant estimate by management in the financial statements and a possibly complex valuation assessment.	We will: ▪ review management's processes and assumptions for their consideration of the fair value of these assets as at 31/3/18. ▪ test any changes to values to ensure they are input correctly into the Authority's records.
Valuation of pension fund net liability	The Authority's net pension fund liability as reflected in its balance sheet represents a significant estimate in the financial statements. .	We will: • identify the controls put in place by management to ensure that the pension fund liability is not materially misstated. We will also assess whether these controls were implemented as expected and whether they are sufficient to mitigate the risk of material misstatement • evaluate the competence, expertise and objectivity of the actuary who carried out your pension fund valuation. We will gain an understanding of the basis on which the valuation is carried out • undertake procedures to confirm the reasonableness of the actuarial assumptions made • check the consistency of the pension fund asset and liability and disclosures in notes to the financial statements with the actuarial report from your actuary.

Other matters

Other work

In addition to our responsibilities under the Code of Practice, we have a number of other audit responsibilities, as follows:

- We carry out work to satisfy ourselves that disclosures made in your Annual Governance Statement are in line with the guidance issued and consistent with our knowledge of the Authority.
- We will read your Narrative Statement and check that it is consistent with the financial statements on which we give an opinion and that the disclosures included in it are in line with the requirements of the CIPFA Code of Practice.
- We carry out work on your consolidation schedules for the Whole of Government Accounts process in accordance with NAO group audit instructions.
- We consider our other duties under the Act and the Code, as and when required, including:
    - giving electors the opportunity to raise questions about your 2017/18 financial statements, consider and decide upon any objections received in relation to the 2017/18 financial statements;
    - issue of a report in the public interest; and
    - making a written recommendation to the Authority, copied to the Secretary of State.
- We certify completion of our audit.

Other material balances and transactions

Under International Standards on Auditing, "irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance and disclosure". All other material balances and transaction streams will therefore be audited. However, the procedures will not be as extensive as the procedures adopted for the risks identified in this report.

Going concern

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). We will review management's assessment of the going concern assumption and evaluate the disclosures in the financial statements.

Group audit scope and risk assessment

In accordance with ISA (UK and Ireland) 600, as group auditor we are required to obtain sufficient appropriate audit evidence regarding the financial information of the components and the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Component	Significant?	Level of response required under ISA (UK and Ireland) 600	Risks identified	Planned audit approach
Mersey Waste Holdings Limited	Yes	Comprehensive	Incomplete or incorrect consolidation	Full scope UK statutory audit performed by Grant Thornton UK

Key changes within the group:

- No changes since prior year identified as part of planning work

Audit scope:

Comprehensive – the component is of such significance to the group as a whole that an audit of the components financial statements is required

Targeted – the component is significant to the Group, audit evidence will be obtained by performing targeted audit procedures rather than a full audit

Analytical – the component is not significant to the Group and audit risks can be addressed sufficiently by applying analytical procedures at the Group level

Materiality

The concept of 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. Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Materiality for planning purposes

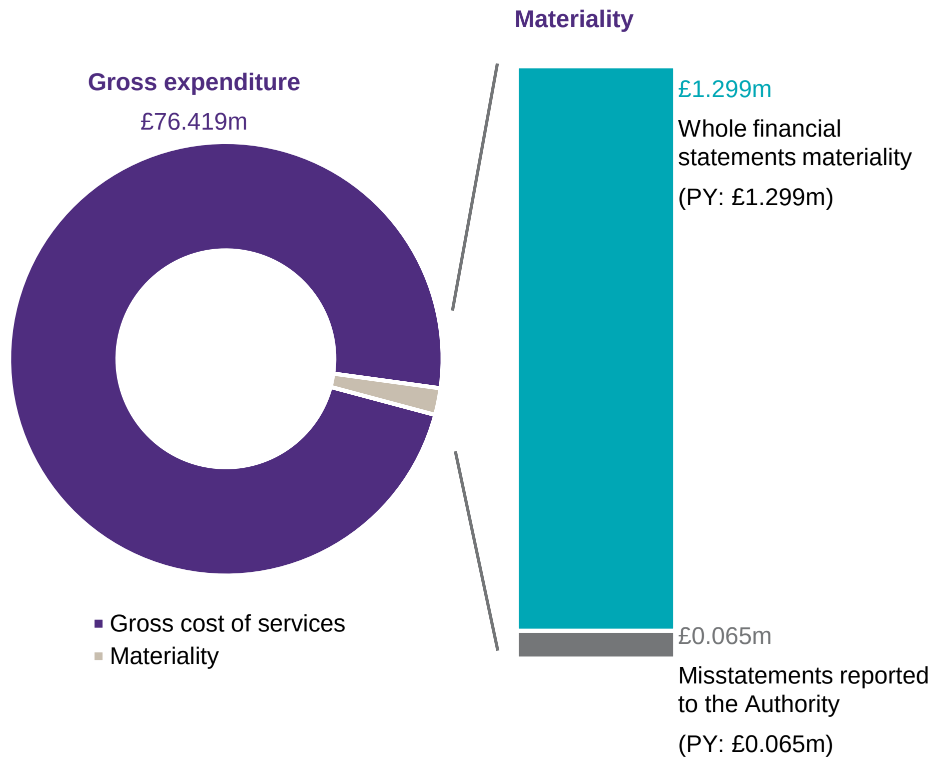
We propose to calculate financial statement materiality based on a proportion of the gross expenditure of the Authority for the financial year. In the prior year we used the same benchmark. We have determined planning materiality (the financial statements materiality determined at the planning stage of the audit) to be £1.299m, which equates to 1.7% of your gross cost of services expenditure for the year (2016/17). We design our procedures to detect errors in specific accounts at a lower level of precision.

We will reconsider planning materiality on receipt of the draft 2017/18 accounts, and if, during the course of our audit engagement, we become aware of facts and circumstances that would have caused us to make a different determination of planning materiality.

Matters we will report to the Authority

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Authority any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work. Under ISA 260 (UK) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 (UK) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.065m (PY £0.065m).

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



Value for Money arrangements

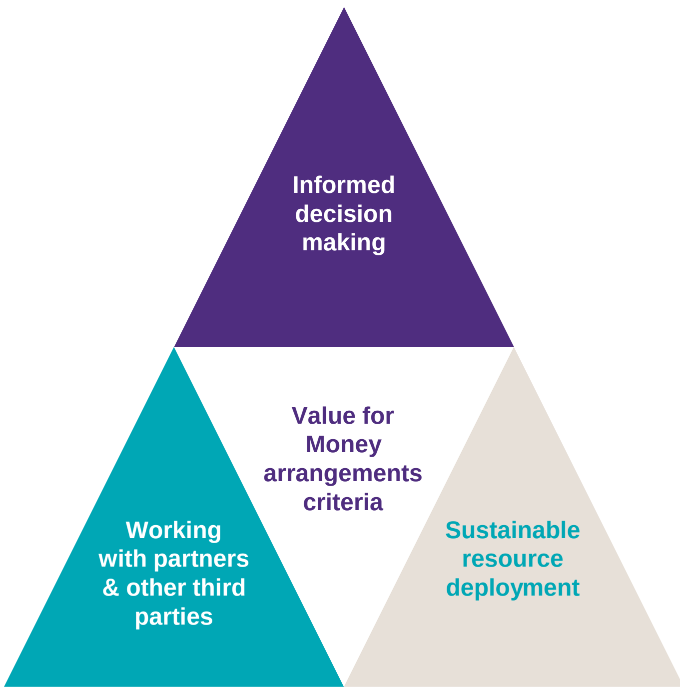
Background to our VFM approach

The NAO issued its guidance for auditors on Value for Money work for 2017/18 in November 2017. The guidance states that for local government bodies, auditors are required to give a conclusion on whether the Authority has proper arrangements in place.

The guidance identifies one single criterion for auditors to evaluate:

"In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people."

This is supported by three sub-criteria, as set out below:



Significant VFM risks

'Those risks requiring specific audit consideration and procedures to address the likelihood that proper arrangements are not in place at the Authority to deliver value for money'.

We set out below the identified significant risk for MWDA.

Authority reserves and levy increases

The Authority continues to operate under significant financial pressures but has continued to manage its finances to deliver a balanced outturn position. However, to avoid levy increases over a number of years, continued use has been made of the Authority's reserves to achieve a balanced budget. This has resulted in general reserves falling to £11.64 million at the end of 2016/17. The planned use of general reserves during 2017/18 is expected to reduce the Authority's available reserves to £2.47m at 31 March 2018. We understand the Authority meeting in February agreed a levy increase of 9% for 2018/19.

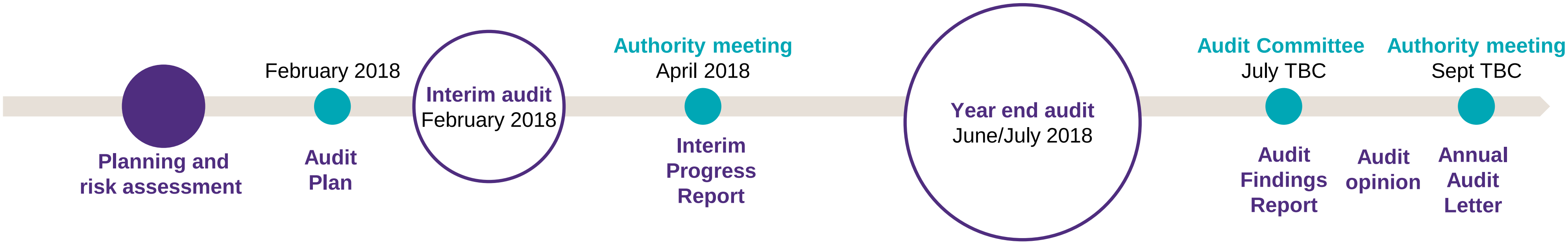
We will continue to monitor the Authority's financial position, in particular the level of general reserves and proposals for levy increases over the medium term.

Resource Recovery Contract

The Resource Recovery Contract became operational on 1 September 2017. Given the significant size of the RRC and the operational impact on the Authority, there is a need for the Authority to ensure effective governance arrangements are in place to manage the contract, including contract variations, review key targets and outputs, monitor budgets and their achievement, as well as ensure effective reporting.

We will discuss with management the governance and contract management, monitoring and reporting arrangements put in place to effectively monitor and report on the RRC.

Audit logistics, team & audit fees



Audit fees

PSAA's indicative fee for the Authority for 2017/18 will be £29,363 (PY: £29,363). We have agreed to keep the Director of Finance updated on any fee implications arising from additional work in connection with the commencement of the Resource Recovery Contract.

Our requirements

To ensure the audit is delivered on time and to avoid additional fees, we have detailed our expectations and requirements in the following section 'Early Close'. If the requirements detailed overleaf are not met, we reserve the right to postpone our audit visit and charge fees to reimburse us for any additional costs incurred.

Early close

Meeting the early close timeframe

Bringing forward the statutory date for publication of audited local government accounts to 31 July this year, across the whole sector, is a significant challenge for local authorities and auditors alike. For authorities, the time available to prepare the accounts is curtailed, while, as auditors we have a shorter period to complete our work and face an even more significant peak in our workload than previously.

We have carefully planned how we can make the best use of the resources available to us during the final accounts period. As well as increasing the overall level of resources available to deliver audits, we have focused on:

- bringing forward as much work as possible to interim audits
- starting work on final accounts audits as early as possible, by agreeing which authorities will have accounts prepared significantly before the end of May
- seeking further efficiencies in the way we carry out our audits
- working with you to agree detailed plans to make the audits run smoothly, including early agreement of audit dates, working paper and data requirements and early discussions on potentially contentious items.

We are satisfied that, if all these plans are implemented, we will be able to complete your audit and those of our other local government clients in sufficient time to meet the earlier deadline.

Client responsibilities

Where individual clients do not deliver to the timetable agreed, we need to ensure that this does not impact on audit quality or absorb a disproportionate amount of time, thereby disadvantaging other clients. We will therefore conduct audits in line with the timetable set out in audit plans (as detailed on page 13). Where the elapsed time to complete an audit exceeds that agreed due to a client not meetings its obligations we will not be able to maintain a team on site. Similarly, where additional resources are needed to complete the audit due to a client not meeting their obligations we are not able to guarantee the delivery of the audit by the statutory deadline. Such audits are unlikely to be re-started until very close to, or after the statutory deadline. In addition, it is highly likely that these audits will incur additional audit fees.

Our requirements

To minimise the risk of a delayed audit or additional audit fees being incurred, you need to ensure that you:

- produce draft financial statements of good quality by the deadline you have agreed with us, including all notes, the narrative report and the Annual Governance Statement
- Compile the group accounts correctly and ensure adequate working papers have been provided to support the group accounts consolidation
- ensure that good quality working papers are available at the start of the audit, in accordance with the working paper requirements schedule that we have shared with you. Please ensure that year end debtor and creditor balances are fully supported by a full analysis of transactions/balances and that there is a full reconciliation between the debtor recorded in the St Helens MBC accounts and the corresponding cash liability recorded in the MWDA accounts
- ensure that the agreed data reports are available to us at the start of the audit and are reconciled to the values in the accounts, in order to facilitate our selection of samples
- ensure that all appropriate staff are available on site throughout (or as otherwise agreed) the planned period of the audit
- respond promptly and adequately to audit queries.

In return, we will ensure that:

- the audit runs smoothly with the minimum disruption to your staff
- you are kept informed of progress through the use of an issues tracker and weekly meetings during the audit
- we are available to discuss issues with you prior to and during your preparation of the financial statements.

Independence & non-audit services

Auditor independence

Ethical Standards and ISA (UK) 260 require us to give you timely disclosure of all significant facts and matters that may bear upon the integrity, objectivity and independence of the firm or covered persons. relating to our independence. We encourage you to contact us to discuss these or any other independence issues with us. We will also discuss with you if we make additional significant judgements surrounding independence matters.

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 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 2016 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

We confirm that we have implemented policies and procedures to meet the requirements of the Ethical Standard. For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Authority.

Fees for other services.

Service	Fees £	Planned outputs
Non-audit related services	None	None

In addition to the above, we have been appointed external auditor to Mersey Waste Holdings Limited where the Authority has an interest.

Service	Fees £
Audit of Mersey Waste Holdings Limited	10,200

Any changes and full details of all fees charged for audit related and non-audit related services by Grant Thornton UK LLP and by Grant Thornton International Limited network member firms will be included in our Audit Findings report at the conclusion of the audit.

Appendices

A. Revised ISAs

Appendix A: Revised ISAs

Detailed below is a summary of the key changes impacting the auditor's report for audits of financial statement for periods commencing on or after 17 June 2016.

Section of the auditor's report	Description of the requirements
Material uncertainty related to going concern	We need to include a brief description of the events or conditions, if any, identified that may cast significant doubt on the Authority's ability to continue as a going concern when a material uncertainty has been identified and adequately disclosed in the financial statements. Under the revised ISA's the auditors report will include a section reporting on the auditors conclusions in relation to going concern.
Other information	We will be required to include a section on other information which includes: • Responsibilities of management and auditors regarding other information • A statement that the opinion on the financial statements does not cover the other information unless required by law or regulation • Reporting inconsistencies or misstatements where identified
Additional responsibilities for directors and the auditor	We will be required to include the respective responsibilities for directors and us, as auditors, regarding going concern.
Format of the report	Under the revised ISAs the format of the auditors report will change and, in particular the opinion section appears first followed by the basis of opinion section.

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