

Audit management letter

for the year ended 31 March 2015 for

Cobtree Manor Estate

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1. Introduction

1.	Introduction	3
2.	Overview	4
3.	Independence	7
4.	Audit scope and objectives	8
5.	Overall audit strategy and approach to significant risks	9
6.	Status of issues raised in prior year	13
7.	Recommendations for the current year	15

Appendices

I.	Agreed accounting adjustments	20
II.	Unadjusted audit differences	21

1. Introduction

This report has been prepared for the trustees of Cobtree Manor Estate (“Cobtree”), to bring attention to those charged with governance various matters arising from the audit of the charity for the year ended 31 March 2015.

Our audit procedures, which have been designed to enable us to express an opinion on the financial statements, have included an examination of the transactions and controls thereon of the charity.

The work we have done was not primarily directed towards identifying weaknesses in the charity’s accounting systems, other than those that would affect our audit opinion, nor to the detection of fraud. We have, however, designed our audit procedures in such a way that we felt would increase our chance of detecting any fraud.

We have included in this report only those matters that have come to our attention as a result of our normal audit procedures and, consequently, our comments should not be regarded as a comprehensive record of all weaknesses that may exist or improvements that could be made.

This report is to be regarded as confidential to the trustees of Cobtree and is intended only for use by them, and the charity’s staff. No responsibility is accepted to any other person in respect of the whole or part of its contents. Before this report, or any part of it, is disclosed to a third party our written consent must be obtained.

The report is designed to include useful recommendations that may help improve performance and avoid weaknesses that could result in material loss to the charity or misstatement of the financial statements and other financial data.

Roles and Responsibilities

The trustees are responsible for the preparation of the financial statements and for making available to us all of the information and explanations we consider necessary. Therefore, it is essential that the trustees confirm that our understanding of all of the matters referred to in this report are appropriate, having regard to their knowledge of the particular circumstances.

2. Overview

Audit Status and overall opinion

We set out below the current status of the audit and our timetable to completion.

We have substantially completed our work, and intend to issue an unmodified audit opinion, subject to the trustees' approving the financial statements and any other minor outstanding items listed below being received and/or completed.

The follow matters are outstanding at the date of this report:

- Final review and approval by you of the final financial statements;
- Agreement of the final financial statements, including the Trustees' Annual Report, to the latest draft;
- Post balance sheet events review to the date of signing the financial statements, including review of latest minutes and management accounts;
- Receipt of signed letter of audit representations.



2. Overview

Independence and ethical standards

We have not identified any potential threats to our independence as auditors. Please see Section 3 for further details.

Audit scope and objectives

We set out the scope and objectives of our audit. See Section 4.

Overall audit strategy

We set out our overall audit approach. See Section 5.

Key audit and accounting issues

We have obtained sufficient, appropriate audit evidence for the significant issues and risks identified during our audit.

During our audit we found no instances of fraud.

Recommendations

We are required to report to you on the significant deficiencies we found in internal controls during the course of our audit, along with any other deficiencies identified.



2. Overview

Misstatements and adjustments to the accounts

It is considered good practice to inform you of any material misstatements within the financial statements presented for audit that have been discovered during the audit. A material misstatement is one where the auditors believe that the misstatement is such as to affect the reader's understanding of the accounts. Materiality is considered in relation to the value of the misstatement and also its context and nature.

The adjustments agreed with you during the course of our audit are shown in Appendix I.

It is generally not practicable to make accounts completely accurate because judgements need to be made and it is difficult to obtain 100% of information about all transactions. Our role is to ensure that deviations from complete accuracy are not material to the reader of the accounts. During the course of our audit we did not identify any unadjusted audit differences.

Going concern

The trustees need to give consideration to the level of reserves maintained, and consider going concern for the period up to at least 31 January 2017, being an estimate of 12 months from the anticipated date of approval of the accounts, and ensure they agree with the assessment. The trustees have confirmed that they believe the financial statements should be prepared on a going concern basis on the grounds that current and future sources of funding or support will be more than adequate for the charity's needs. Our review supports the going concern status of the charity.

Thanks

We would like to take this opportunity to thank Maidstone Borough Council for the assistance afforded to us during the course of the audit.



3. Independence

Under current UK Ethical Standards we are required as auditors to confirm our independence to “those charged with governance” i.e. the trustees.

Our internal procedures are designed to ensure that all partners and professional staff are aware of relationships that may be considered to bear on our objectivity and independence as auditors.

The procedures require that audit engagement partners are made aware of any matters which may reasonably be thought to bear on the firm’s independence and the objectivity of the audit engagement partner and the audit staff. This document considers such matters in the context of our audit for the year ended 31 March 2015.

In addition to performing the statutory audit, we also provide the following non-audit services:

Service	Possible threat	Safeguards
VAT advice	Self-review	The VAT advice is provided by our tax partner, Brian Carey, who has no involvement in the audit process.



4. Audit scope and objectives

Our statutory audit of the financial statements is carried out in accordance with International Standards on Auditing (UK and Ireland) of the statutory financial statements, with the aim of forming an opinion whether:

The financial statements give a true and fair view of the state of the charity's affairs as at 31 March 2015 and of the result for the year then ended.

The financial statements have been properly prepared in accordance with UK GAAP.

The financial statements have been prepared in accordance with the requirements of the Charity SORP.

The information given in the Trustees' Report for the financial year is consistent with the financial statements.

We also report on whether:

The charity company has kept adequate accounting records.

The financial statements are in agreement with the accounting records and returns.

Other information contained in the annual report is not consistent with the audited financial statements.

Certain disclosures of trustees' remuneration specified by law are not made.

We have not received all the information and explanations we require for our audit.



5. Overall audit strategy

Risk-based audit

We performed a risk-based audit, focussing our work on key audit areas. We began by developing an understanding of the charity's activities and the specific risks it faces. We held an initial planning meeting with key management and finance staff to ascertain management's own view of potential audit risk, and to gain an understanding of the activities. We have also developed an in depth understanding of the accounting systems and controls so that we may ensure their adequacy as a basis for the preparation of the financial statements, and that proper accounting records have been maintained.

Our audit procedures were carried out, and then we ensured the presentation and disclosure in the accounts meet all the necessary requirements.

Significant risks

As part of our audit procedures we are required to consider the significant risks that require special audit attention.

Auditing Standards require us to consider:

- Whether there is a risk of fraud;
- Whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;
- The complexity of transactions;
- Whether the risk involves significant transactions with related parties;
- The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and
- Whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual.



5. Overall audit strategy

The identified significant audit risks were communicated to you in our audit planning report issued before our main fieldwork began. We now note the work performed and conclusions drawn on the following pages:

Significant risk	Explanation of the risk	Audit work performed	Conclusion
<p>Revenue recognition (mandatory risk)</p>	<p>The auditor's responsibility is to conduct the audit on the basis that there is an assumption that revenue recognition is a fraud risk.</p> <p>Work is therefore required to ensure that all income is recognised appropriately and in line with the charity's accounting policies and the charity SORP.</p> <p>We are also required to confirm that income has been correctly classified between restricted and unrestricted funds.</p>	<p>Obtain an understanding of all sources of income, and any contracts or terms & conditions attached.</p> <p>Sample testing income, verifying to supporting documentation to ensure income has been recognised in the correct period.</p> <p>Cut off testing around the period-end to ensure all income is included in the relevant period.</p> <p>Review to ensure that income has been correctly classified between restricted and unrestricted funds, reviewing any terms and conditions etc.</p> <p>Analytical review.</p>	<p>A material error was identified in relation to other income, and a prior year adjustment has also been necessary to strip out income reflected in 2013/14 from brought forward funds.</p> <p>See Appendix I for more details.</p>



5. Overall audit strategy

Significant risk	Explanation of the risk	Audit work performed	Conclusion
<p>Management override (mandatory risk)</p>	<p>The trustees and other management have the primary responsibility for the detection of fraud, as an extension of their role in preventing fraudulent activity. Trustees should ensure a sound system of internal controls is in operation to support these, and other, objectives.</p> <p>Auditing Standards presume a significant risk of management override of the system of internal controls, because management can often find themselves in a unique position where they could potentially override routine day to day financial controls.</p> <p>Our audit is designed to provide reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or error.</p> <p>We are not responsible for preventing fraud or corruption, although our audit may serve to act as a deterrent.</p>	<p>Management often find themselves in a unique position where potentially could override routine day to day financial controls.</p> <p>Our audit considers this risk and we adapt our procedures accordingly.</p> <p>During our audit we considered the possibility of manipulation of financial results, for example through the use of journals or management estimates, such as provisions and accruals.</p>	<p>Our audit procedures have not identified any instances of management override.</p>



5. Overall audit strategy

Significant risk	Explanation of the risk	Audit work performed	Conclusion
<p>Treatment of capital expenditure on the new buildings as a direct cost charged to the Statement of Financial Activities</p>	<p>In the 2014 accounts a significant sum (£370k) was spent on the new building works. This was treated as an expense for the year, rather than being capitalised on the Balance Sheet.</p> <p>This looks strange at first glance, and potentially means that fixed and net assets are understated.</p>	<p>Review of the work to date to understand fully the nature of the works being carried out.</p>	<p>The treatment of capital expenditure, both in the current and previous years, has been incorrect.</p> <p>It has been agreed with Paul Holland, that the capital expenditure costs of £963k should be capitalised on the Balance Sheet.</p> <p>As the amounts involved in previous years are so significant (£666,882) a prior period adjustment was required.</p>
<p>Non-depreciation of freehold buildings</p>	<p>Where the accounting policy is not to depreciate it is necessary to complete an annual impairment review to consider the carrying value of the buildings.</p> <p>Due to the absence of depreciation there is a risk that the carrying value of the property is overstated.</p> <p>If this were to be the case funds will also be overstated.</p>	<p>Review and analysis of any impairment review undertaken.</p>	<p>No impairment review was carried out by the charity.</p> <p>However from our own impairment review carried out, the non-depreciation of freehold buildings appears appropriate.</p>



5. Overall audit strategy

Significant risk	Explanation of the risk	Audit work performed	Conclusion
<p>Classification as income and expenditure between restricted and unrestricted funds</p>	<p>The 2014 accounts included a large balance of £463k shown as unrestricted 'other income', some of which appears to relate to capital grants.</p> <p>It is possible that some of this funding was incorrectly classified as unrestricted since there may have been terms and conditions attached.</p>	<p>Review of any terms and conditions attached to incoming resources in both the current and prior years, to ensure income is correctly classified.</p> <p>Review of expenditure allocated against restricted funds to ensure that costs treated in this way meet the relevant criteria to be matched against restricted income.</p>	<p>The donations received for the costs of building have incorrectly been treated as unrestricted funds.</p> <p>This has been corrected in the final accounts.</p>



6. Status of audit issues raised in prior year

This section updates you on the status of the issues your previous auditors brought to your attention last year, and confirms whether any further action is required.

Issue (& Cause)	Solution suggested	Follow up comments, including whether further action required
<p>The charity was made aware of the current statutory audit thresholds.</p> <p>Furthermore attention was drawn to the fact that, historically, the Corporate Trustee has taken the decision to appoint auditors. This decision was made taking into account of any independence issues raised by the Charity Commission.</p>	<p>It was noted that the Charity intends to continue this practice in future years.</p>	<p>No further points to note.</p>



7. Recommendations for the current year

Significant deficiencies in internal control

We are required to report to you, in writing, significant deficiencies in internal control that we have identified during the audit. These matters are limited to those which we have concluded are of sufficient importance to merit being reported to you. As the purpose of the audit is for us to express an opinion on the charitable company's financial statements, you will appreciate that our audit cannot necessarily be expected to disclose all matters that may be of interest to you and, as a result, the matters reported may not be the only ones which exist. As part of our work, we considered internal control relevant to the preparation of the financial statements such that we were able to design appropriate audit procedures. This work was not for the purpose of expressing an opinion on the effectiveness of internal control.

We confirm that we have identified a significant deficiency in internal control during the 2015 audit and this is explained in detail below.

Area	Observation	Recommendations	Management response
 <p>High</p> <p>General charity records</p>	<p>During the audit we had significant difficulty in trying to agree the amounts included in the accounts and as a result had to spend a considerable amount of time in reworking the 2015 accounts to a position where we were comfortable with the figures.</p> <p>There is a distinct lack of an audit trail and this is mainly down to the fact that the charity's records are so intrinsically linked to MBC records that the accounts are effectively created from the council ledger and spreadsheets. This therefore appeared to result in some amounts being included in the charity's accounts as a balancing figure in order to get MBC's books to agree.</p>	<p>We would strongly recommend that MBC set up the charity's own accounting records. This could be done by way of a spreadsheet or alternatively it may be easier to use a simple piece of accounting software.</p> <p>This would enable MBC to record the double entry of all transactions which relate to the charity, even if the transaction goes through the MBC bank account.</p> <p>To do this a MBC loan/intercompany account would need to be set up in the charity's records and every time a CME transaction goes through the MBC bank account then an entry can be made to the loan account, with a corresponding debit to expenditure or credit to income.</p> <p>If something similar is set up in MBC then, as a double check, the two loan accounts should always agree.</p>	



7. Recommendations for the current year

We are also required to communicate other significant audit findings such:

- where we consider a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate in the particular circumstances of the entity;
- significant difficulties, if any, encountered during the audit; or
- other matters, if any, arising from the audit that, in our professional judgement, are significant to the oversight of the financial reporting process are communicated to those charged with governance.

We have had some difficulties, with these mainly arising due to the treatment of certain items in previous years.

It has been necessary to advise the need for three significant prior year adjustments. These are explained in the notes to the accounts, but are also explained below:

- (1) to increase brought forward funds by £666,882 for capital assets that were expended as costs for the year in 2014 and 2013;**
- (2) the 2014 SOFA included other incoming resources of £463,145, but it has become apparent that these were included here in error due to a misunderstanding of certain accounting treatments. Total incoming resources for 2014 have therefore been reduced by £463,145 and restated to £332,274.**
- (3) the 2014 Statement of Financial Activities (“SOFA”) originally included a loss on investment assets of £363,069. A prior year adjustment for £509,304 has been made to leave a gain of £146,235 in the restated 2014 SOFA. £506,000 of this adjustment related to a disposal of fixed asset investments in 2014 which had incorrectly been reflected in the SOFA. The remaining £3,304 corrects a historical difference.**

A further smaller prior adjustment was also needed to leave the correct balance on brought forward funds, and this is explained in the notes to the accounts. In total the prior year adjustments have been increased from a previously stated £3,764,342 to £4,484,876.



7. Recommendations for the current year

Other deficiencies in internal control

We also bring to your attention other deficiencies that came to our attention during our work, again along with our recommendations, and your own response:



Low

Medium risk/priority



Med

Low risk/priority

	Risk/Issue	Area	Observation	Recommendations	Management response
1.	 Med	Capital expenditure	<p>As part of our audit testing it was identified that capital costs of £963k for the visitor centre, Kent Life and playground had not been capitalised, instead incorrectly being treated as an income and expenditure item.</p> <p>A significant part of the £963k related to previous years, resulting in a prior period adjustment being required.</p> <p>Furthermore an additional capital accrual was identified as part of our after date invoice review.</p>	<p>In future we recommend that you carefully review any potential capital costs to ensure that they are treated correctly in the accounts.</p> <p>Any capital items that are deemed to be a work in progress should be treated as 'assets under construction'.</p> <p>It is recommended that material after date invoices received are reviewed to ensure that all amounts relating to 31 March are included in the accounts.</p>	



7. Recommendations for the current year

	Risk/Issue	Area	Observation	Recommendations	Management response
2.	 Med	Unincorporated legal status of the charity	<p>The charity is structured as an unincorporated trust, with no limited liability for the corporate trustee, Maidstone Borough Council.</p> <p>Whilst there can be some benefits from operating through such a structure, most charities of any size, or those with staff, will operate through a corporate structure, such as a limited by guarantee company or a charitable incorporated organization (CIO).</p> <p>There are various risks associated with continuing with the current set up:</p> <p>(a) The corporate trustee is personally liable in relation to contracts entered into on behalf of the trust and will remain so even once they cease to be trustees unless the contract is terminated or novated. Any indemnity will not assist them if the charitable funds are insufficient, even if they have acted perfectly properly. This will include employment contracts for staff.</p> <p>(b) The charity has no legal status of its own, and cannot be sued. The corporate trustee's assets are therefore potentially at risk since any individual or organization taking legal action would do so against the corporate trustee, and not the charity itself.</p>	<p>We recommend you give consideration to changing the legal structure of the charity, and consider both the limited by guarantee company and new CIO structure.</p> <p>There are pros and cons of both structures, and we would be pleased to explain these to you in more detail.</p> <p>As a minimum we recommend that you ensure each of the trustees fully understands the implications of the current structure, and that this is communicated to all potential new trustees so that they are aware of the legal responsibilities.</p>	



7. Recommendations for the current year

	Risk/Issue	Area	Observation	Recommendations	Management response
3.	 Med	VAT	<p>As noted in the independence section, we have been asked to carry out a VAT review, separate to the audit.</p> <p>This VAT review and the report issued to you identified that the all sources of income received during the year were exempt from VAT.</p> <p>Therefore even if the charity were voluntarily registered for VAT, input VAT would not be able to be reclaimed on purchases as they are deemed to be exempt supplies.</p> <p>We noted from our audit testing that Maidstone Borough Council have been claiming input VAT on the charity's behalf for a number of years, and we believe that this is incorrect.</p> <p>We have not been able to quantify the amount involved but it is likely to be substantial.</p>	<p>We would recommend that Maidstone Borough Council stop reclaiming input VAT on the charity's behalf with immediate effect.</p> <p>We would also advise that you seek professional advice to quantify the amount likely to be recovered by HMRC.</p>	
4.	 Med	Fund accounting	<p>The charity has received some donations that were received specifically for capital purposes, however this income has been incorrectly recognised through the general unrestricted funds.</p>	<p>It would be normal for any income (grants or donations) received specifically for capital purposes to be allocated to a restricted fixed asset fund.</p> <p>This helps to ensure that the capital income is spent in line with the purposes intended.</p>	



7. Recommendations for the current year

	Risk/Issue	Area	Observation	Recommendations	Management response
5.	 Low	Fixed assets	<p>It was noted during our fixed assets testing that an impairment review had not been carried out.</p> <p>Where the accounting policy is not to depreciate it is necessary to complete an annual impairment review to consider the carrying value of the buildings.</p>	<p>In order to ensure that the carrying value of the property is not overstated, it is important that the charity carries out an annual impairment review.</p> <p>This should be done in advance of the audit fieldwork.</p>	
6.	 Low	MBC creditor	<p>Due to the number of changes made to the original accounts presented for audit, it was difficult to agree the year end MBC council to third party supporting documentation.</p> <p>Ideally there should be an easy way of agreeing and identifying the balance in the MBC accounts especially as it is such a significant number.</p>	<p>This is linked to the point raised re: the inadequacy of the charity's records so please see the significant deficiencies in internal control section.</p>	



7. Recommendations for the current year

The new charity SORP

There are also a number of points which we wish to bring to your attention in respect of the new charities SORP, which will apply to your next financial year end, 31 March 2016. Where necessary the comparative figures will need to be restated, and the opening balance position for the comparatives (1 April 2014) restated.

There are actually two new charity SORPs: one for larger charities (the FRS 102 SORP) and one for charities (the FRSSE SORP) which qualify as small. Cobtree Manor Estate is comfortably within the small charity thresholds and so will be able to adopt the FRSSE SORP, if you wish to do so.

Are there any benefits in opting for Charities SORP FRSSE?

Charities SORP FRS 102 generally requires more detailed disclosures than Charities SORP FRSSE, in particular for intangible fixed assets, investments, stock, financial instruments, liabilities, pension schemes, accounting policies, trustee and staff remuneration (including termination payments) and related party transactions. However there are few significant variations.

One such variation is that under the SORP FRSSE donated tangible fixed assets must be included at current value, whereas under SORP FRS 102 these must be recognised at fair value.

Note: The FRSSE is due to be withdrawn in the near future, and so any charity that initially opts to apply Charities SORP FRSSE will have to implement further changes to their accounting policies and future accounts at this point in time. It may therefore make sense to opt to prepare accounts in accordance with the SORP FRS 102 initially.

What will change under SORP FRS 102?

- You will be required to explain the financial effect of significant events, in addition to reporting the significant charitable activities undertaken;
- Instead of a statement on risk management you will need to provide a description of the principal risks and uncertainties facing the charity, together with a summary of your plans and strategies for managing those risks;



7. Recommendations for the current year

What will change under SORP FRS 102? - continued

- Arrangements for setting the pay and remuneration of the charity's key management personnel and any benchmarks, parameters or criteria used in setting their pay, will need to be disclosed;
- The governance costs heading in the SOFA is no longer relevant, and the costs that you have previously included in here, such as legal and professional costs, will need to be included within support costs;
- Under the new accounting framework, income is recognised if a charity has entitlement to the income, the likelihood of receipt is probable and the amount can be reliably measured.

Under the current framework income is recognised when the likelihood of receipt is 'virtually certain'. It may therefore be possible to account for some elements of your income in an earlier period than previously.

- The definition of related parties has been expanded to include key management personnel. As a result, the total remuneration and expense reimbursement for your senior management will need to be disclosed, and additional details are now required in respect of redundancy and termination payments;
- A holiday pay accrual will need to be included in the financial statements, if material. Under the current reporting regime this is optional. The accrual is accounted for by reference to the amount of untaken holiday at the year end, multiplied by the rate of pay for that individual. You may therefore wish to consider aligning your holiday year with the accounting year, if these two periods do not already coincide. (SORP FRS 102 only)
- Income categories introduced for the first time in Charities SORP 2005 have been replaced by five broad headings of income from Donations and legacies, Charitable activities, Other trading activities, Investments and Other.
- More detailed disclosures for income from government grants.
- The total amount of individual donations without conditions made by trustees will need to be disclosed (individual amounts do not).



8. Appendix I - Agreed accounting adjustments

A significant number of differences have been identified during the audit and posted to the statutory accounts, following agreement with your key management:

	Effect on brought forward funds £
<i>Prior year adjustments</i>	
Certain qualifying fixed assets not capitalised in prior periods	665,946
Income incorrectly included due to misunderstanding of certain accounting treatments	(463,145)
Incorrect treatment of investment assets	509,304
Other historical differences re: opening balances of funds at 1 April 2013	8,429
Total impact of prior year adjustments on funds brought forward at 1.4.14	<u>720,534</u>
Funds per previous filed 2013/14 accounts	3,764,342
Restated funds at 1.4.14 following above prior year adjustments	4,484,876



8. Appendix I - Agreed accounting adjustments

Other adjustments agreed

	£	Effect on 2015 net income £
Removal of previously accumulated surpluses incorrectly included in other income	93,526	(93,526)
Correcting of capital expenditure incorrectly included in Income & Expenditure	296,508	296,508
Correcting gains/(losses) on investment assets	3,766	(3,766)
Additional capital accrual identified	50,781	-
		<u>199,216</u>

Reconciliation between draft accounts presented for audit and final accounts

Net surplus per original accounts	286,134
UHY adjustments above	199,216
	<u>485,350</u>



9. Appendix II – Unadjusted audit differences

We are required to bring to your attention audit adjustments that the trustees are required to consider. We confirm that no such adjustments were identified.

