

REPORT TO THE BOARD OF DIRECTORS OF

Southend Care Ltd

Audit of the Financial Statements

For the Period Ending 31 March 2018





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- LETTER OF REPRESENTATION



1. Introduction and Coverage

- 1.1 This report summarises our key findings in connection with the audit of the financial statements of Southend Care Ltd in respect of the period ended 31 March 2018.
- 1.2 The scope of our work was set out in our Audit Plan which was presented to the Board of Directors on 31 July 2018.
- 1.3 It should be noted that the matters identified in this management letter arose from the conduct of our normal audit procedures which are designed primarily to enable us to express an opinion on the financial statements of Southend Care Ltd and do not necessarily involve an examination of all aspects of your internal control procedures. The responsibility for maintaining adequate financial reporting systems and systems of internal control, as well as for the prevention and detection of fraud, irregularities and other errors, rests with management.
- 1.4 Consequently, the comments in our management letter cannot be regarded as a complete analysis of all weaknesses or irregularities in the system of internal control.
- 1.5 Our duties as financial statements auditors do not specifically include searching for fraud or other irregularities although our audit was planned so as to have a reasonable expectation of detecting material mis-statements within the financial statements.
- 1.6 Our work also included a review of the adequacy of disclosures in the financial statements and consideration of the appropriateness of the accounting policies and estimation techniques adopted by the company.



2. Financial Performance – Profit and Loss Account

2.1 RESULTS

- 2.1.1 The financial statements are for the 11 month period ended 31 March 2018. The previous financial statements were for the Company's first period following their incorporation and covered the period of 21 April 2016 to 30 April 2017. The Company commenced trading on the 1 April 2017 and the prior periods financial statements only show the results for the month of April 2017.
- 2.1.2 After excluding the IAS19 adjustments for the defined contribution pension liability, Southend Care Ltd's financial performance in 2017/18 shows a loss for the period of £24,936 compared to a loss in 2016/17 of £258,830.
- 2.1.3 The impact of the adjustment for the IAS19 defined benefit pension scheme charge of £535,000 is to increase the deficit to £559,936.

2.2 INCOME

- 2.2.1 Revenue for the 11 month period totalled £5,421,212.
- 2.2.2 Block funding income totalled £5,313,745 for the 11 months to 31 March 2018.
- 2.2.3 Other income represents the sale of meals, intensive one to one sessions and contributions from Essex County Council for the shared lives employment service.



2. Financial Performance – Profit and Loss Account (Continued)

2.3 EXPENDITURE

2.3.1 Expenditure, excluding pension scheme adjustments under (IAS19), totalled £5,446,148 for the 11 months to 31 March 2018.

2.3.2 Staff costs totalled £4,859,924, this is broken down as follows:

	£
Wages	3,491,549
Employer's NI	306,536
Employer's pension	549,312
Recruitment	20,633
Training	3,290
Agency	488,604
Total	<u>£ 4,859,924</u>

2.3.3 Administrative expenses totalled £549,765 in the period. this is broken down as follows:

	£
Premises costs	146,904
Transport costs	25,063
Supplies and services	263,939
Third party payments	5,857
Irrecoverable VAT	122,005
Implementation costs	(14,003)
Total	<u>£ 549,765</u>

Implementation costs are a negative figure in the financial statements for the period. Last year they were shown inclusive of VAT instead of net which has resulted in an adjustment for the VAT amount this year.



3. Financial Position – Balance Sheet

3.1 CASH AT BANK

3.1.1 Cash at bank has increased by £146,408 to £496,158. The increase of available cash is a result of additional support from Southend-on-Sea Borough Council by way of additional implementation loan and an increase in creditors at the period end.

3.2 PENSION SCHEME DEFICIT

3.2.1 A number of Southend-on-Sea Borough Council employees were transferred to Southend Care Ltd in three tranches on 1 April 2017, 1 July 2017 and 1 October 2017. In accordance with IAS19 this has resulted in the recognition of the corresponding defined benefit pension scheme liability in respect of the Local Government Pension Scheme.

3.2.2 At the date of the first transfer (1 April 2017) the pension scheme liability totalled £2.640m, the comparatives for the period ended 30 April 2017 have been restated to recognise this liability. During the period ended 31 March 2018 the pension scheme deficit has increased by £2.858m leaving a pension scheme deficit at 31 March 2018 of £5.498m. The assumptions used by the actuary are as follows:

	31 March 2018
Rate of increase in salaries	3.8%
Rate of increase in pensions	2.3%
Discount rate	2.6%

3.3 RELATED PARTY TRANSACTIONS

3.2.3 At the period end the following balances were outstanding with the Company's parent entity Southend-on-Sea Borough Council:

- Debtor £548,428
- Short term creditor £543,271
- Long term creditor working capital £350,000
- Long term creditor £214,573



4. Going Concern

4.1 GOING CONCERN REVIEW

- 4.1.1 The Company relies on the financial support from Southend-on-Sea Borough Council, its parent, during its start-up and the initial loss making period.
- 4.1.2 On review of the 10 year Financial Business Plan, the Company forecast that they will make profits from 2020/2021. This coincides with their plans for a new Care Home and Day Centre on Burr Hill Chase. In the run up to this period the Company will rely on Southend-on-Sea Borough Council to provide any working capital required.
- 4.1.3 Southend-on-Sea Borough Council have provided written confirmation that they will continue to provide financial support to the Company. It is expected that the Company will repay the working capital and implementation loan within the next 5 years.

4.2 CONCLUSION

- 4.2.1 We agree with the going concern assessment made by the Company and will therefore be giving an unqualified audit opinion on the financial statements for the period ended 31 March 2018.



5. Audit and Accounting Issues to be reported to the Board of Directors

5.1 PROCEDURAL RECOMMENDATIONS

Audit Finding	Risk Identified	Recommendation	Management Response
<p>Personnel Files</p> <p>During our payroll testing we identified that the Human Resources department archive personnel files once an employee has ended their employment and no electronic copies of documents are stored. It takes 6 weeks to recover files from archiving.</p> <p>In addition, during our testing the Human Resources department could not locate a particular personnel file.</p> <p>Human Resources were unsure as to whether the file has been mislaid or not set-up on employment.</p>	<p>There is a risk that documents on a leavers personnel file may be needed post-employment and will not be readily available.</p> <p>It is a legal requirement to retain certain employment related documents for all of your current employees.</p>	<p>We recommend undertaking a review of your personnel files to ensure that files are maintained for all of your current staff and these are easily traceable.</p> <p>We recommend that the Human Resources department either maintains electronic copies of leaver forms, or does not archive personnel files until after the year end audit has been completed.</p>	



5. Audit and Accounting Issues to be reported to the Board of Directors (Continued)

5.1 PROCEDURAL RECOMMENDATIONS (CONTINUED)

Audit Finding	Risk Identified	Recommendation	Management Response
<p>VAT</p> <p>During the course of the audit it was identified that there was a difference between the Company's actual turnover and the turnover declared on the VAT returns for the period. It was also identified that some of this income was not included in the irrecoverable VAT calculation.</p> <p>The accounting team provided schedules with explanations of the differences and confirmations that these will not provide a material adjustment to the period end VAT liability. We have not undertaken a full review of these workings and your VAT records.</p>	<p>There is a risk that irrecoverable VAT will be incorrectly calculated and the Company will owe HMRC further input VAT.</p> <p>There is a risk that the VAT liability is incorrectly calculated on the VAT spreadsheets.</p> <p>There is the risk that providing HMRC with incorrect figures on the VAT returns could trigger a VAT investigation.</p>	<p>We recommend that the figures entered into boxes 6 and 7 on the VAT returns are reconciled to the accounting records on a quarterly basis.</p> <p>We recommend that the figures entered onto the partial exemption calculation are reconciled to the accounting records on a quarterly basis.</p> <p>We recommend that the VAT team rework the partial exemption calculation for the twelve months to 31 March 2018 and pay over any understatement in irrecoverable VAT.</p>	



5. Audit and Accounting Issues to be reported to the Board of Directors (Continued)

5.1 PROCEDURAL RECOMMENDATIONS (CONTINUED)

Audit Finding	Risk Identified	Recommendation	Management Response
<p>Share Capital Base</p> <p>The losses of the Company are being financed by the long term loans from Southend on Sea Borough Council and the Company is being supported by this debt instead of its share capital.</p> <p>The Company is incurring annual interest charges at 7% of the long term debt.</p>	<p>There is a risk that the Company will not be able to repay the loan within the 5 year period initially expected.</p> <p>The Company's losses are being increased by the annual interest charge, creating the risk of additional financial pressure.</p>	<p>We recommend that SBC consider whether the capital structure of the Company is appropriate, in the instance that the losses are expected to continue and the Company will find it difficult to repay the loan.</p>	



5. Audit and Accounting Issues to be reported to the Board of Directors (Continued)

5.1 PROCEDURAL RECOMMENDATIONS (CONTINUED)

Audit Finding	Risk Identified	Recommendation	Management Response
<p>Accounting Treatment of Trading Balances with SBC</p> <p>During the course of our audit it was identified that 'short term debtors owed by SBC' were reintroduced as sales in period April 2018. This resulted in a duplicate of the original transaction as they are also recognised as sales in March 2018. These amounts were later reversed on receipt of the money from SBC, though this could result in a timing difference if this receipt is recognised in a different accounting period.</p>	<p>There is a risk that management decisions are made on review of figures produced for April 2018 that include turnover also recognised in March 2018.</p> <p>There is a risk that these transactions are included in the VAT and partial exemption calculations for April 2018.</p>	<p>We recommend that following the year end the amounts posted to the nominals used to manage the year end SBC balances (BB530 and BB412) are reinstated to the appropriate accounts receivable and accounts payable codes and are not posted through the profit and loss account.</p>	



5. Audit and Accounting Issues to be reported to the Board of Directors (Continued)

5.1 PROCEDURAL RECOMMENDATIONS (CONTINUED)

Audit Finding	Risk Identified	Recommendation	Management Response
<p>Suspense Account</p> <p>During the course of our audit we identified a significant number of transactions posted to suspense account 9999.</p> <p>In many instances transactions were being miscoded by the individual posting the transaction onto the accounting system which resulted in an automatic default to this account. A member of the accounts staff then had to review the account and clear it down at the year end.</p>	<p>There is a risk that transactions will remain miscoded when misposted to the suspense account.</p> <p>Staff resources are being used to undertake a review of this account and repost transactions to their correct nominal.</p>	<p>We recommend that suspense account 9999 is reviewed monthly and all accounting staff are advised to not post transactions to this account.</p> <p>We recommend that all staff involved in posting transactions on to the accounting system are provided with a schedule of recommended nominal ledger codes for each type of transaction to assist them in their posting.</p>	



5. Audit and Accounting Issues to be reported to the Board of Directors (Continued)

5.2 TAXATION

- 5.2.1 The company is subject to corporation tax on its taxable profits. During the year (and the previous period) the company has made losses which can be carried forward and used against taxable profits. Provision can be made for a deferred tax asset in regards to these losses, but we would recommend that this is not done until there is a greater certainty of taxable profits to offset the losses.

As a local authority trading company Southend Care Ltd can apply for a corporation tax dispensation, if the company continues to only trade with local authorities. This would result in profits not being subject to corporation tax. We have been advised that the company's intent is to expand and trade with private entities so this dispensation will not be available.



6. Independence

- 6.1 In accordance with International Standard on Auditing (UK and Ireland) 260 “Communication of audit matters with those charged with governance“, there are no changes to the details of relationships between Scrutton Bland LLP and its related entities and Southend Care Ltd and its related entities that may reasonably be thought to bear on Scrutton Bland LLP’s independence and the objectivity of the audit principal, Timothy O’Connor and the audit staff and the related safeguards from those disclosed in the Audit Plan presented to the Company on 31 July 2018.



7. Conclusions

- 7.1 The 2017/18 financial statements audit has been conducted in accordance with the audit plan prepared for the Board of Directors and presented to the Company. We are pleased to report that no significant matters came to our attention during the course of our audit that led us to deviate from our plan.
- 7.2 We would like to take this opportunity once again to thank the Paul Grout and his staff, and other senior management and staff for the considerate help and assistance we have been given in carrying out our audit.

Scrutton Bland LLP

22 August 2018

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Dear Sirs

We confirm that the following representations are made on the basis of enquiries of management and staff with relevant knowledge and experience and where appropriate, of inspection of supporting documentation, sufficient to satisfy ourselves that we can properly make each of the following representations to you in connection with your audit of the company's financial statements for the period ended 31 March 2018.

We acknowledge our legal responsibilities regarding disclosure of information to you as auditors and confirm that so far as we are aware, there is no relevant audit information needed by you in connection with preparing your audit report of which you are unaware. Each director has taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that you are aware of that information.

1. We acknowledge, and have fulfilled, as directors, our collective responsibility under the Companies Act 2006 for presenting financial statements (in accordance with the Companies Act 2006 and International Financial Reporting Standards), which give a true and fair view of the financial position of the company at the reporting date, and of its result for the period then ended, and for making accurate representations to you. We confirm that we have approved the financial statements for the period ended 31 March 2018.
2. We confirm that the accounting policies and estimation techniques adopted for the preparation of the financial statements are the most appropriate to the circumstances in which the company operates.

3. Other than as disclosed in the financial statements, the company has not entered into any transactions involving directors, officers or other related parties, which require disclosure under the Companies Act or International Financial Reporting Standards. Appropriate disclosure has been made of the control of the company.
4. We have disclosed all known or possible litigation and claims whose effects should be considered when preparing the financial statements and these have been disclosed in accordance with the requirements of International Accounting Standards.
5. The financial statements of the company have been prepared on the going concern basis as we believe that adequate cash resources will be available to cover the company's requirements for working capital and capital expenditure for at least the next twelve months. We are not aware of any other factors which could put into jeopardy the company's going concern status during or beyond this period.
6. There have been no events since the reporting date which necessitate revision of the figures included in the financial statements or inclusion of a note thereto. Should further material events occur, which may necessitate revision of the figures included in the financial statements or inclusion of a note thereto, we will advise you accordingly.
7. We confirm that we have considered the unadjusted errors advised to us by you as appended to this letter. It is our view that the cost of making these adjustments to the financial statements outweighs any benefits that will be gained by the users of the financial statements. The combined effect of the unadjusted errors is not material and we do not consider that their absence from the financial statements affects the true and fair view given.
8. We confirm that we have agreed the adjustments appended to this letter which have been made to the performance statement(s) and balance sheet which we presented to you for audit.
9. We confirm we have no plans or intentions that may materially affect the carrying value or classification of any assets and liabilities reflected in the financial statements.
10. We confirm that after the audit report has been signed, we will circulate a copy of our financial statements to every member of the company, every holder of the company's debentures and every other person entitled to receive notice of general meetings, as required by section 423, Companies Act 2006.
11. With regard to the defined benefit pension plan, we are satisfied that:
 - the actuarial assumptions underlying the valuation are consistent with our knowledge of the business;

- all significant retirement benefits have been identified and properly accounted for; and
 - all settlements and curtailments have been identified and properly accounted for.
12. We confirm that we are part of a group in the UK, headed by Southend-on-Sea Borough Council and that the group financial statements are consolidated under IFRS.
13. We confirm that it is correct to restate the comparatives to include the following:
- A debtor for unpaid share capital of £100
 - The defined benefit pension scheme liability relating to the transfer of staff on 1 April 2017 totalling £2.64m.
14. We confirm that it is not appropriate to recognise a deferred tax asset in the financial statements until there is a greater certainty that the company will make profits.
15. We confirm that our accounting system does not allow transactions to be deleted.

Information provided:

16. All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the company have been properly reflected and recorded in the accounting records. We have provided to you all other information requested and given unrestricted access to persons within the entity from whom you have deemed it necessary to speak to. All other records and relevant information, including minutes of all management and shareholders' meetings, have been made available to you.
17. Other than those disclosed in the financial statements we are not aware of any material liabilities, provisions, contingent liabilities, contingent assets or contracted for capital commitments, that need to be provided for or disclosed in the financial statements.
18. The company has satisfactory title to all assets and there are no liens or encumbrances on the company's assets.
19. We confirm that the functional currency of the company is Sterling.
20. We confirm that we have notified you of all related party relationships, and transactions that the company has entered into with those related parties during the period of which we are aware.
21. We acknowledge our responsibility for the design and implementation of internal controls to prevent and detect errors or fraud, and have disclosed to you the results

of our assessment of the risk that the financial statements may be materially misstated as a result of fraud. We are unaware of any irregularities, including fraud and suspected fraud, involving management, employees or others who have significant roles in internal control, or those employed by the company where the fraud could have a material effect on the financial statements. No allegations of such irregularities or breaches have come to our notice.

22. We are unaware of any breaches or possible breaches of statute, regulations, contracts, agreements or the company's Memorandum and Articles of Association which might result in the company suffering significant penalties or other loss. No allegations of such irregularities or breaches have come to our notice.
23. We confirm that we have been notified by you that there are no matters which you are required to raise with us to comply with your profession's ethical guidance which are in addition to the matters included in your external audit plan.
24. We confirm that we wish to take advantage of the applicable small company exemptions in accordance with the provisions of the Companies Act 2006.
25. We confirm that we have been notified by you that there are no matters which you are required to raise with us to comply with your profession's ethical guidance which are in addition to the matters included in your assignment terms letter to us.
26. We confirm receipt of your external audit plan and we confirm receipt of your management letter.

Yours faithfully

Signed on behalf of the board of directors

Date

SOUTHEND CARE LTD**Unadjusted errors within Company Financial Statements****Period ended 31 March 2018**

	Balance Sheet		I & E	
	Dr	Cr	Dr	Cr
Accruals		9,850		
Accountancy fees expense			9,850	
Being inclusion of creditor for our fees for the period ended 31 March 2018.				
		- 9,850	9,850	-
Effect on company retained profit			<u>9,850</u>	

SOUTHEND CARE LTD**Adjusted errors within Company Financial Statements****Period ended 31 March 2018**

	Balance Sheet		I & E	
	Dr	Cr	Dr	Cr
B/f pension reserve	2,640,000			
B/f pension scheme liability		2,640,000		

Being introduction of ISA18 pension scheme deficit into comparative accounts- no client posting required (relates to restatement of 2016 financial statements)

Debtors	100			
Share capital		99		
Investments		1		

Being introduction of debtor for unpaid share capital and restating share capital value – no client posting required (relates to restatement of 2016 financial statements)

	<u>2,640,100</u>	<u>2,640,000</u>	<u>-</u>	<u>-</u>
Effect on company retained profit			<u>0</u>	