



Annual Audit Letter

Ashfield District Council
Year ending 31 March 2019





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1. EXECUTIVE SUMMARY

Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor for Ashfield District Council for the year ended 31 March 2019. Although this letter is addressed to the Council, 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 responsibility	Summary
Audit of the financial statements	<p>Our auditor's report issued on 31 July 2019 included our opinion that the financial statements:</p> <ul style="list-style-type: none">• give a true and fair view of the Council's financial position as at 31 March 2019 and of its expenditure and income for the year then ended; and• have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19.
Other information published alongside the audited financial statements	<p>Our auditor's report issued on 31 July 2019 included our opinion that:</p> <ul style="list-style-type: none">• The other information in the Statement of Accounts is consistent with the audited financial statements.
Value for Money conclusion	<p>Our auditor's report concluded that we are satisfied that in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.</p>
Reporting to the group auditor	<p>In line with group audit instructions issued by the NAO, we reported to the group auditor in line with the requirements applicable to the Council's WGA return.</p>
Statutory reporting	<p>Our auditor's report confirmed that we did not use our powers under s24 of the 2014 Act to issue a report in the public interest or to make written recommendations to the Council.</p>

2. AUDIT OF THE FINANCIAL STATEMENTS

Opinion on the financial statements

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 Council and whether they give a true and fair view of the Council's financial position as at 31 March 2019 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 (ISAs). These require us to consider whether:

- the accounting policies are appropriate to the Council'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 auditor's report, issued to the Council on 31 July 2019, stated that, in our view, the financial statements give a true and fair view of the Council's financial position as at 31 March 2019 and of its financial performance for the year then ended.

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 Audit Committee. We call this our trivial threshold.

The table below provides details of the materiality levels applied in the audit of the main financial statements for the year ended 31 March 2019. A slightly higher materiality level applies for the group accounts.

Financial statement materiality	Our financial statement materiality is based on 2% of Gross Revenue Expenditure at a Surplus/Deficit on Provision of Services level	£1,714k
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£51k
Specific materiality	We applied a lower level of materiality to the following areas of the accounts: <ul style="list-style-type: none"> • Officers Remuneration • Termination Payments • Members Allowances • Audit Fee 	£5,000 per individual officer £76k £77k £9k

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2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Our response to significant risks

As part of our continuous planning procedures, we considered whether there were risks of material misstatement in the Council's financial statements that required special audit consideration. We reported significant risks identified at the planning stage to the Audit Committee in 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.

Identified significant risk	Our response	Our findings and conclusions
<p>Management override of controls</p> <p>Management at various levels within an organisation 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 override could occur there is a risk of material misstatement due to fraud on all audits.</p>	<p>We addressed this risk by performing audit work in the following areas:</p> <ul style="list-style-type: none"> • Documenting our understanding of the processes and controls in place to mitigate the risks identified; • Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements; • Evaluating the business rationale for any significant transactions outside the course of the business; • Understanding the oversight given by those charged with governance of management processes over fraud; • Making enquiries of management and Internal Audit regarding actual or any suspicions of fraud; and • Considering whether the Council's accounting policies are consistent with industry standards. 	<p>There were no matters arising from our work on management override of controls</p>
<p>Valuation of property, plant and equipment</p> <p>The Council's accounts contain material balances relating to its holding of property, plant and equipment, investment properties and assets held for sale, with the majority of land and building assets required to be carried at valuation. Due to the high degree of estimation uncertainty associated with those held at valuation, we determined there was a significant audit risk in this area.</p>	<p>We addressed this risk through:</p> <ul style="list-style-type: none"> • Reconciling valuations from the valuer's report to those recorded in the Fixed Asset Register; • Testing a sample of assets valued during the year to valuation reports; • Where material, testing the basis for impairment of assets, the value and correct accounting treatment; • Critically assessing the Council's valuer's scope of work and methodology used; and • Considering the impact of any assets not valued during the year. 	<p>There were no significant issues arising from our work and we were satisfied the valuation of property, plant and equipment was materially correct.</p>

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Identified significant risk	Our response	Our findings and conclusions
<p>Defined benefit liability valuation</p> <p>The Council's accounts contain material liabilities relating to the local government pension scheme. The Council uses an actuary to provide an annual valuation of these liabilities in line with the requirements of IAS 19 Employee Benefits. Due to the high degree of estimation uncertainty associated with this valuation, we determined there was a significant risk in this area.</p>	<p>We addressed this risk through:</p> <ul style="list-style-type: none"> • Reviewing the appropriateness of the Pension Asset and Liability valuation methodologies applied by the Pension Fund Actuary, and the key assumptions included within the valuation. This included comparing them to expected ranges, utilising information provided by the consulting actuary engaged by the National Audit Office; • Agreeing the data in the IAS 19 valuation report provided by the Fund Actuary for accounting purposes to the pension accounting entries and disclosures in the Council's financial statements. • Critically assessing the competency, objectivity and independence of the Nottinghamshire Pension Fund's Actuary, Barnett Waddingham; • Liaising with the auditors of the Nottinghamshire Pension Fund to gain assurance that the controls in place at the Pension Fund are operating effectively. This included the processes and controls in place to ensure data provided to the Actuary by the Pension Fund for the purposes of the IAS 19 valuation is complete and accurate; and • Performing a walkthrough of payroll transactions at the Council to understand how pension contributions which are deducted and paid to the Pension Fund by the Council. 	<p>Our work provided the assurance sought and we were satisfied the local government pensions liability was not materially misstated. All local authorities have been affected by an accounting issue that impacts the value of pension liabilities. Two on-going legal cases (Guaranteed Minimum Pensions and McCloud/Sergeant) have created uncertainty over whether pension liabilities are fairly stated. The Council's actuary (via the Pension Fund) did not make an allowance in its actuarial valuation for either of these cases and early guidance given to councils was that the impact would not be material. The Council, as with nearly all local authorities in England, prepared the financial statements on this basis. In our view, these cases give rise to at least a constructive obligation, which is required to be recognised under IAS 19. As a result the Council obtained a revised valuation from the Pension Fund via its actuarial expert incorporating these two issues.</p>

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

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	<u>Bank reconciliations</u> Through our bank testing it was identified that the working paper to support the reconciliation of the cash figures could not be immediately reconciled. This resulted in a difference at year-end between bank accounts and ledger on the supporting working paper by £84. The Council has since identified the reconciling item but the exercise should have been completed at the year end.
Potential effects	Working papers which don't reconcile can cause delays.
Recommendation	The Council should ensure that supporting working papers agree to the bank and ledger and that reconciling items are investigated promptly.
Management response	Agreed.

Description of deficiency	<u>Related parties</u> Due to the local elections in May, five former Members failed to return their related party declarations.
Potential effects	Related party declarations could be incomplete.
Recommendation	Whilst there are extenuating circumstances in an election year, the Council should ensure that it has all related party returns in future years.
Management response	Agreed.

Description of deficiency	<u>Land registry</u> During our property, plant and equipment testing, we identified some land that the Council owns but that was not formally registered with the Council.
Potential effects	The Council is open to disputes over unregistered land.
Recommendation	The Council is undertaking an exercise to register all its land with the land registry and should conclude this as soon as possible.
Management response	Agreed.

3. VALUE FOR MONEY CONCLUSION

Value for Money conclusion

Unqualified

Our approach to Value for Money

We are required to consider whether the Council has 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 Council 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 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 Value for Money work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Council being inadequate. In our Audit Completion Report, we reported that we had identified two significant Value for Money risks. The work we completed in relation to the significant audit risks is outlined on the following page, which supported our auditor's report, issued to the Council on 31 July 2019, that, in all significant respects, the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31st March 2019.

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3. VALUE FOR MONEY CONCLUSION (CONTINUED)

Significant Value for Money risks

Risk	Work undertaken	Conclusion
<p>The continual pressures on local government finances are well documented and the Council has experienced a significant decrease in government grant funding since 2010/11. In response to the projected future budget deficits caused by these falling central government funding levels and increases in service demands, the Council has established a Transformation Plan focusing on modernising services, innovation and better use of technology. The Council has set a balanced budget for 2018/19, anticipating utilising reserves and achieving transformation savings. The current forecast is a small surplus for the year on the General Fund and a larger surplus on the Housing Revenue Account . The medium term financial plan (MTFP), covering the period from 2019/20 to 2023/24, forecasts a deficit of around £2 million per year, before the delivery of savings. The budget is based on a number of assumptions around inflation, business rates income and pay increases. There is a risk that the Council will not generate sufficient new income streams and deliver projected savings from transformation which are crucial in bridging the budget gap whilst meeting its strategic priorities.</p>	<p>We have critically reviewed whether the Council has considered:</p> <ul style="list-style-type: none"> • funding reductions; • business rate reform; • fair funding; • salary and general inflation; • demand pressures; • restructuring costs; and • sensitivity analysis given the degree of variability in the above factors. <p>We reviewed the delivery of savings in 2018/19 and progress to identify savings for 2019/20 – 2023/24 and evaluated the impact on the Council's revenue reserves.</p>	<p>Having completed our planned procedures, we are satisfied that the Council has adequate arrangements for securing economy, efficiency and effectiveness in its use of resources. It has a robust Medium Term Financial Plan (MTFP) and has clearly presented the financial challenges facing the organisation and the sector. It has laid out plans for the next three years, including potential budget gaps, modelling a potential cumulative gap of up to £4 million by 2021/22 . Specifically, the MTFP details the assumptions which have been made in developing the Plan and these are reasonable. They include:</p> <ul style="list-style-type: none"> • Salary and inflationary increases, including separate assumptions for utility and non utility inflation • Council tax • Business rates and levels of provision for appeals • Levels of Government funding including Revenue Support Grant, Business Rates Retention and New Homes Bonus <p>The MTFP also highlights areas where outcomes are still unknown such as changes in national and local policy and the results of the Fair Funding review</p> <p>The projected level of reserves to 2023/24 remain to be steady with minimal deviation. The Council's aim is to not tap into reserves and use income for funding. The General Fund minimum balance is maintained at its current level and is not called upon for other purposes. The Council has delivered the target level of savings for 2018/19.</p>

5. VALUE FOR MONEY CONCLUSION (CONTINUED)

Risk

Work undertaken

Conclusion

The 2018/19 year end position was a £1.148 million surplus against budgets, and the Council was able to increase general fund reserves by £3.637m in year. This further strengthened the Council's already robust position with regard to reserves, taking usable reserves to £52 million overall with general fund reserves of £6 million and earmarked reserves of almost £8 million within this balance. The Council is therefore in a good position but will need to keep the emphasis on its investment decisions and income generation in order to bridge the gap in funding for future years.

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5. VALUE FOR MONEY CONCLUSION (CONTINUED)

Risk	Work undertaken	Conclusion
Investments in commercial property		
<p>The Council has identified the use of its capital and treasury activities as one way of generating new income streams. The Council spent £14.98 million on investment properties in 2017//18 with the expectation that they will generate annual rental income of over £1 million rental income. In 2018/19, the Council has purchased a further investment property for £4.33 million which is expected to generate annual rental income of £0.29 million, with plans for further expenditure of £6 million approved for the year.</p> <p>Whilst the investment decisions are projected to deliver optimised financial returns with both revenue and capital growth, the strategy presents a significant value for money risk in considering whether the Council has exposed itself to risks that it has not anticipated, including:</p> <ul style="list-style-type: none"> • Poor financial forecasting; • Insufficient commercial expertise; and • Poor investment decisions due to insufficient legal and due diligence work. 	<p>We have critically reviewed whether the Council has:</p> <ul style="list-style-type: none"> • Exposed itself to too much financial risk through its borrowing and investment decisions; • Ensured that it has been mindful of changes in the accounting and regulatory environment when undertaking any sensitivity analysis as part of its investment decision making process; • Ensured that an appropriate level of legal and due diligence work has been undertaken prior to making specific investment decisions; • Responded appropriately to the revised Statutory Guidance on Local Government Investments, to ensure that there is appropriate transparency to understand the exposure that the Council has as a result of its borrowing and investment decisions; and • Ensured that Members have sufficient expertise to understand the complex transactions that they have ultimate responsibility for approving. 	<p>The Capital Strategy has been presented to Council as a Policy Framework document with links to the Treasury Management Strategy, Medium Term Financial Strategy (MTFS) and the Corporate Asset Management Plan. The Capital Strategy (and specifically the Commercial Investment Strategy element of the Capital Strategy) are key drivers to secure the future financial sustainability of the Council. The Council is committed to further acquisitions of commercial properties in future years and, following two reviews by Internal Audit, it has strengthened its governance processes, specifically:</p> <ul style="list-style-type: none"> • Including the risk around commercial property acquisitions in the corporate risk register • Committing to a performance monitoring dashboard for commercial property investments • Reporting to Members on an annual basis • Developing a training programme for Members on commercial property acquisitions, some of which has already been delivered, with plans to train new Members in the coming months. • Taking a cautious approach at the identification and due diligence stage to property acquisition.

4. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	No matters to report
Completion of group audit reporting requirements	Consistent
Other information published alongside the audited financial statements	Consistent

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

Matters on which we report by exception

The 2014 Act provides us with specific powers where matters come to our attention that, in our judgement, require reporting action to be taken. We have the power to:

- Issue a report in the public interest
- Make a referral to the Secretary of State where we believe that a decision has led to, or would lead to, unlawful expenditure, or an action has been, or would be unlawful and likely to cause a loss or deficiency; and
- Make written recommendations to the Council which must be responded to publicly.

We have not exercised any of these statutory reporting powers.

Reporting to the NAO in respect of Whole of Government Accounts consolidation data

The NAO, as group auditor, requires us to complete the WGA Assurance Statement in respect of its consolidation data. We submitted this information to the NAO in accordance with their deadline.

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 Council. In our opinion, the other information in the Statement of Accounts is consistent with the audited financial statements.

5. OUR FEES

Fees for work as the Council's auditor

We reported our proposed fees for the delivery of our work in the Audit Strategy Memorandum, presented to the Audit Committee in March 2019.

Having completed our work for the 2018/19 financial year, we can confirm that our final fees are as follows:

Area of work	2018/19 proposed fee	2018/19 final fee
Delivery of audit work under the NAO Code of Audit Practice	£43,148	£43,148
Total	£43,148	£43,148

6. FORWARD LOOK

Audit Developments

Code of Audit Practice

The Code of Audit Practice sets out what local auditors of relevant local public bodies are required to do to fulfil their statutory responsibilities under the Local Audit and Accountability Act 2014. We have responded to the National Audit Office's consultation on the content of the Code (<https://www.nao.org.uk/code-audit-practice/about-code/>).

A new Code will be laid in Parliament in time for it to come in to force no later than 1 April 2020.

Financial Resilience

Fair Funding Review

The Council will need to incorporate the outcome of the Spending Review, due in the latter half of 2019, to its Medium Term Financial Plan. The Spending Review will set out the department allocations for 2020/21 and potentially beyond. Regardless of the timing and period covered by the Spending Review, the Council recognises the key issue is the management of general reserves to a level that ensures it remains financially resilient and able to deliver sustainable services. It must, therefore, ensure it clarifies and quantifies how it will bridge the funding gap through planned expenditure reductions and/ or income generation schemes.

Local Authority Financial Resilience Index

CIPFA is moving forward with its financial resilience index, which it believes will be a barometer on which local authorities will be judged. We would expect the Council to have at least considered the index once it is formally released.

Commercialisation

The National Audit Office will be publishing a report on Commercialisation during 2019. Depending on the Council's appetite for Commercialisation, we would expect the Council to consider the outcome of the report and ensure any lessons learnt are incorporated into business practice.

Further, the UK Debt Management Office's Annual Report, published on 23 July 2019, reported that, as at 31 March 2019, the Public Works Loan Board's loan book was £78.3 billion with 1,308 new loans totalling £9.1 billion advanced during the year. As a result, we expect local authorities to clearly demonstrate:

- the value for money in the use of Public Works Loan Board funds to acquire commercial property; and
- the arrangements for loan repayment through the updated Statutory Guidance on Minimum Revenue Provision in 2019/20, 2020/21 and beyond.

Financial Reporting

UK Local Government Annual Accounts

The CIPFA/LASAAC Local Authority Code Board specifies the financial reporting requirements for UK local government. A consultation is underway to inform the direction and strategy for local government annual accounts. We will be submitting our response and suggest practitioners also voice their opinion.

Lease accounting

The implementation of IFRS 16 Leases in the Code is delayed until 1 April 2020. The Council will need a project plan to ensure the data analysis and evaluation of accounting entries is completed in good time to ensure any changes in both business practice and financial reporting are captured.

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6. FORWARD LOOK (CONTINUED)

Next year's audit and how we will work with the Council

We will focus our work on the risks that your challenges present to your financial statements and your ability to maintain proper arrangements for securing value for money.

In the coming year we will continue to support the Council by:

- continued liaison with the Council's Internal Auditors to minimise duplication of work;
- attending Audit Committee meetings and presenting an Audit Progress Report including updates on regional and national developments; and
- hosting events for staff, such as our Local Government Accounts workshop.

We will meet with the Council to identify any learning from the 2018/19 audit and will continue to share our insights from across local government and relevant knowledge from the wider public and private sector.

In terms of the technical challenges that officers face around the production of the statement of accounts, we will continue to work with them to share our knowledge of new accounting developments and we will be on hand to discuss any issues as and when they arise.

The Council has taken a positive and constructive approach to our audit and we wish to thank Members and officers for their support and co-operation during our audit.

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