Agenda Item No 4(b)

DERBYSHIRE COUNTY COUNCIL

AUDIT COMMITTEE

24 September 2019

Report of the Director of Finance & ICT

ANNUAL AUDIT LETTERS 2018-19

1 Purpose of the Report

To provide Members with details of the external auditor's Annual Audit Letters for 2018-19.

2 Information and Analysis

The Council's external auditor, Mazars, is required to present an Annual Audit Letter to Members and officers of the Council. The letter describes the scope of the audit work for the financial year and reports on matters of significance arising from that work. It is a summary of its conclusions and provides an external assessment of the Council's overall financial position.

The letter is a means by which the appointed auditor fulfils its statutory requirements, which are derived from the Audit Commission Act 1998 and the Audit Commission's Code of Audit Practice. The external auditor is required to provide an opinion on the Council's financial statements and a conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources.

The issuing of the letter, along with an audit certificate, marks the end of the audit process for 2018-19. The Council has published on its website that the audit has been concluded in accordance with the Accounts and Audit Regulations 2015.

The letters issued for the Council and the Pension Fund are attached at Appendix 1A and Appendix 1B.

The details contained within the letter have been reported to the Audit Committee previously.

3 Considerations

In preparing this report the relevance of the following factors has been considered:- financial, human resources, legal and human rights, equality of opportunity, health, environmental, transport, property, crime and disorder and social value considerations.

4 Background Papers

Papers held in Technical Section, Finance & ICT Division, Room 137.

5 Officer's Recommendation

That Audit Committee notes the details of the Annual Audit Letters 2018-19.

PETER HANDFORD

Director of Finance & ICT

Annual Audit Letter

Derbyshire County Council

Year ended 31 March 2019

CONTENTS

1. EXECUTIVE SUMMARY

Purpose of the Annual Audit Letter

Our Annual Audit Letter summarises the work we have undertaken as the auditor for Derbyshire County 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	Our auditor's report issued on 31 July 2019 included our opinion that the financial statements: • 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	Our auditor's report issued on 31 July 2019 included our opinion that: • the other information in the Statement of Accounts is consistent with the audited financial statements.
Value for Money conclusion	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.
Reporting to the group auditor	In line with group audit instructions issued by the NAO, on 23 August 2019 we reported to the group auditor in line with the requirements applicable to the Council's Whole of Government Accounts return.
Statutory reporting	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. We received a question from a local elector that we agreed to treat as a formal objection. Our consideration of the matters raised by the elector took place in August 2018, with a planned conclusion date of 28 September. We are unable to issue the Audit Certificate until at least that date.

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 financial statements for the year ended 31 March 2019:

Financial statement materiality	Our financial statement materiality is based on 2% of Gross Revenue Expenditure at a Surplus/Deficit on Provision of Services level	£31.169m
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£0.935m
Specific materiality	We applied a lower level of materiality to the following areas of the accounts:	
	• Officers' Remuneration	£5,000 per individual officer
	• Termination Payments	£374,000
	• Members' Allowances	£215,000
	• Audit Fee	£23,000

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
Management override of controls 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.	We addressed this risk by performing audit work in the following areas: • 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 process 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.	There were no matters arising from our work on management override of controls.
Expenditure recognition Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council (FRC), which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. Having considered the factors for expenditure recognition, we believe the risk is focused on the year-end balance sheet and in particular the completeness and valuation of manually accrued payables. Due to the nature and/or value of expenditure on employee expenses, interest payments, depreciation, impairments and loss on disposal of assets; we do not believe the risk lies in those balances; but the risk is relevant to premises, transport, and supplies & services.	We addressed this risk by: • ensuring the accounting policies in relation to expenditure recognition and recognition of accruals were appropriate and consistently applied; • testing year end creditors to confirm that they had been correctly valued and categorized and were correctly treated as a creditor of the authority; and • carrying out cut-off testing, and testing for unrecorded liabilities, to confirm expenditure had been coded to the correct accounting year.	Our work has not identified any material errors in the financial statements.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Identified significant risk	Our response	Our findings and conclusions
Revenue recognition Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. Having considered the factors for revenue recognition, we believe the risk is focused on the year-end balance sheet and in particular the existence and accuracy of receivables, specifically those that are material, subject to manual intervention and/or significant estimation. Due to the nature and/or value of income from interest and investment income, council tax, business rates and government grants we do not believe the risk lies in those balances, but the risk is relevant to fees, charges and other service income.	We addressed this risk by: • ensuring the accounting policies in relation to revenue recognition and recognition of accruals are appropriate and consistently applied; • testing year end debtors to confirm that they have been correctly valued and categorized and are correctly treated as a debtor of the authority; and • carrying out cut-off testing to confirm income has been coded to the correct accounting year.	Our work has not identified any material errors in the financial statements.
Valuation of property, plant and equipment 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.	We addressed this risk through: • 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.	The procedures we have undertaken have not identified any material errors or uncertainties in the financial statements.

2. AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Identified significant risk	Our response	Our findings and conclusions
Defined benefit liability valuation 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.	We addressed this risk through: • 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 Derbyshire Pension Fund's Actuary, Hymans Robertson; • liaising with the auditors of the Derbyshire 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.	Our work provided the assurance sought and we were satisfied the local government pensions liability was not materially misstated.

2. AUDIT OF THE FINANCIAL STATEMENTS

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	**Controls in place in regard to the valuation process -** Our 2018/19 testing of land and buildings valuations identified a number of issues, but did not identify any material errors. These issues included a misclassification of agricultural land as residential land, the omission of a school building and an inconsistent approach to the valuation of homes for older people. We do however acknowledge that management has taken steps to correct and address these matters together with the deficiencies identified in 2017/18 and has introduced a valuation manual to improve the accuracy and consistency of the valuation work undertaken.
Potential effects	Valuable assets are held by the Council. Inaccurate valuation or indexation can therefore result in large errors. This increases the risk of the Property, Plant and Equipment figure being materially misstated on the Council's Balance Sheet. For 2018/19 we did however obtain sufficient evidence to conclude the Property, Plant and Equipment figure for 2018/19 was materially correct.
Recommendation	The Council has taken steps to address the deficiencies identified in relation to the valuation of land and buildings, however it should now embed the processes set out in its valuation manual to ensure that valuation work is appropriately completed and checked on a timely basis to enable accurate entries to be made in the pre-audit statement of accounts.
Management response	Agreed. The valuation manual is a living document utilised by the asset valuation team to ensure effective valuation delivery. The team will focus on fully embedding the processes set out in the manual.

Description of deficiency	**Controls in place in regard to contracts of employment -** During our payroll testing it became apparent that management could not locate the contracts of employment for 2 members of staff.
Potential effects	Contracts of employment are important documents that may be required to clarify terms and conditions of employment or to provide supporting information in relation to grievances or disputes. Not having access to such information could be prejudicial to the Council.
Recommendation	The Council should ensure that contracts of employment are held and are accessible in relation to all members of staff.
Management response	Management accept the recommendation and acknowledges the importance of contractual documentation. The two cases identified related to employees who work and are employed by Schools and therefore the Shared Services Centre do not hold the full employee file for the employee as this is the responsibility of the School to retain. Procedures for logging and sending paper documentation for employees within Schools who purchase the traded services package offsite will be reviewed in line with the HR retention schedule to ensure that an accurate record is maintained within the Shared Services Centre for all future documentation generated.

Internal control recommendations (continued)

Description of deficiency	**Controls in place in regard to the completeness of related party declarations -** During our testing of related parties it was found that three councillors had not declared their membership of another public sector body.
Potential effects	Whilst there were no inherent conflicts of interest involved and it is acknowledged that this may simply have been an oversight, good practice encourages full disclosures to ensure transparency.
Recommendation	The Council should ensure that full disclosures are made and should emphasise the importance of full disclosures during the training sessions associated with the implementation of the Council's new constitution.
Management response	Agreed. The Council's new constitution came into effect on 15 May 2019 and the importance of full disclosures will form part of the training sessions associated with the new constitution.

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 not identified any significant risks to our VFM conclusion. We did though identify one specific matter which we needed to keep to under close review: The work we completed in relation to this matter is outlined below, 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.

Significant Value for Money risk

Risk	Work undertaken	Conclusion
Financial sustainability – The Council continues to face financial pressure in the coming years and the Council keeps updating its medium term financial plan (MTFP) to meet these pressures. We needed to ensure our knowledge of the Council's MTFP arrangements and its monitoring of the planned delivery of savings, remained up to date in order to ensure we gave the correct VFM conclusion.	We have assessed whether any matters have come to our attention through the course of our audit that lead us to conclude that a risk to our 2018/19 VFM conclusion does indeed exist. We addressed this requirement by reviewing the Council's arrangements for developing and delivering its MTFP and for working in partnership.	We obtained sufficient assurance to conclude that the Council continues to have appropriate arrangements in place.

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 statutory recommendations that must be considered and responded to publicly;
- apply to the court for a declaration that an item of account is contrary to law; and
- issue an advisory notice under schedule 8 of the 2014 Act.

We have not exercised any of these statutory reporting powers.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account. We received one such objection or question and have undertaken work to ensure that the matters involved do not have a material impact in relation to our opinion on the financial statements or VFM conclusion.

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 on 23 August 2019.

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.

We have completed our work for the 2018/19 financial year, but at the time of producing this report, we have not yet finalised our audit fees for the year. We carried out additional audit work to address the risk of material misstatement on the Council's pension liability, arising from the actuarial impact of GMP and McCloud, resulting in an additional fee of £750. In addition, we have proposed an additional fee of £3,500 for the work undertaken in relation to an objection we received from a local elector. These fee variations require the approval of Public Sector Audit Appointments Limited, before finalising the audit fee.

Area of work	2018/19 proposed fee	2018/19 final fee ***
Delivery of audit work under the NAO Code of Audit Practice	£96,524 plus VAT	£100,774 plus VAT

*** Please note that at the time of producing this report, the audit fee has not yet been finalised.

Fees for non-PSAA work

At the present time we have not been separately engaged by the Council to carry out additional work outside of the fees in relation to our appointment by PSAA. Before agreeing to any non-PSAA work we will confirm there were no actual, potential or perceived threats to our independence.

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.

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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MAZARS

Annual Audit Letter

Derbyshire Pension Fund

Year ended 31 March 2019

Derbyshire Pension Fund

MAZARS

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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 Derbyshire Pension Fund for the year ended 31 March 2019. Although this letter is addressed to the members of Derbyshire County Council, as a body and as administering authority for the Derbyshire Pension Fund, 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	Our auditor's report issued on 31 July 2019 included our opinion that the financial statements: • give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2019 and the amount and disposition of the fund's assets and liabilities as at 31 March 2019; 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	Our auditor's report issued on 31 July 2019 included our opinion that: • the other information in the Statement of Accounts is consistent with the audited financial statements.
Statutory reporting	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 Pension Fund.
Consistency Report	We have yet to issue our consistency report setting out that in our opinion the Pension Fund financial statements within the Pension Fund's Annual Report are consistent with the Pension Fund financial statements within the Statement of Accounts of the Council. We will issue our audit certificate once this work is completed.

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 Pension Fund and whether they give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2019 and the amount and disposition of the fund's assets and liabilities as at 31 March 2019.

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 Pension Fund'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 on 31 July 2019, stated that, in our view, the financial statements give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2019 and the amount and disposition of the fund's assets and liabilities as at 31 March 2019.

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.

We set overall materiality at the planning stage of the audit at £46m using a benchmark of 1% of net assets available to pay benefits. Our final assessment of overall materiality, based on the final financial statements is £49m using the same benchmark.

We set our trivial threshold (the level under which individual errors are not communicated to the Audit Committee) at £1.4m based on 3% of overall materiality.

Performance materiality is the amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce, to an appropriately low level, the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. In setting performance materiality we have taken into account that this is our first year of audit and accordingly we do not hold extensive cumulative audit knowledge about the Pension Fund's financial statements. We have therefore set our performance materiality at 65% of our overall materiality being £32m.

The table below provides details of the materiality levels applied in the audit of the financial statements for the year ended 31 March 2019:

Financial statement materiality	Our financial statement materiality is based on 1% of net assets available to pay benefits	£49m
Performance materiality	Our performance materiality is based on 65% of our financial statement materiality	£32m
Trivial threshold	Our trivial threshold is based on 3% of financial statement materiality.	£1.4m

Our response to significant risks

As part of our continuous planning procedures, we considered whether there were risks of material misstatement in the Pension Fund'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
Management override of controls 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.	We addressed this risk by performing audit work in the following areas: • accounting estimates impacting on amounts included in the financial statements; • consideration of identified significant transactions outside the normal course of business; and • journals recorded in the general ledger and other adjustments made in preparation of the financial statements.	There were no matters arising from our work on potential areas of management override of controls.
Valuation of unquoted investments for which a market price is not readily available As at 31 March 2018 the fair value of investments which were not quoted on an active market was £634m (£844m as at 31 March 2019), which accounted for 14% (17% as at 31 March 2019) of the Fund's net investment assets. Inherently these assets are harder to value, as they do not have publicly available quoted prices from a traded market, and as such they require professional judgement or assumptions to be made when valuing them at year end. As the pricing of these investment assets is subject to judgements, they may be susceptible to pricing variances due to the assumptions underlying the valuation. We therefore considered that there was an increased risk of material misstatement.	In addition to our standard programme of work in this area we have: • agreed the valuations to supporting documentation including investment manager valuation statements and cash flows for any adjustments made to the investment manager valuations; • agreed the investment manager valuations to audited accounts. Where these were not available, we agreed the investment manager valuation to other independent supporting documentation; • where audited accounts were available, we checked that they were supported by a clear opinion; and • where available, we reviewed any independent control assurance reports and confirmed that they do not highlight any risks of material misstatement.	Our work has provided the assurance we sought and has not highlighted any material errors or uncertainties in the financial statements.

Internal control recommendation

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 deficiency in internal control as part of our audit.

Description of deficiency	**Controls in place in regard to pensions payroll to general ledger reconciliations** The SAP payroll and general ledger provide an integrated system. However achieving a reconciliation between the payroll and ledger entries took more management and audit time than anticipated this year and emphasised the value of having regular reconciliations in place between the information in the pensions payroll reports and the SAP general ledger to avoid such problems for the future.
Potential effects	Whilst the absence of this reconciliation does not indicate that an error has occurred this reconciliation is an important check that the general ledger information populated from pensions payroll is complete and accurate.
Recommendation	Whilst acknowledging that management has taken steps to address this issue for 2018/19 we recommend that pensions payroll to general ledger reconciliations are undertaken, reviewed and authorised on an ongoing basis.
Management response	Agreed. The Pension Fund will review, develop and implement a reconciliation process during 2019/20.

We also followed up on the internal control recommendations raised by KPMG in relation to 2017/18 and re-raised any outstanding actions required.

3. OTHER REPORTING RESPONSIBILITIES

Exercise of statutory reporting powers	**No matters to report**
Consistency Report - the Pension Fund financial statements within the Pension Fund's Annual Report are consistent with the Pension Fund financial statements within the Statement of Accounts of the Council	**We have yet to issue our consistency report. We will issue our audit certificate once this work is completed.**
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 Pension Fund'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 statutory recommendations that must be considered and responded to publicly;
- apply to the court for a declaration that an item of account is contrary to law; and
- issue an advisory notice under schedule 8 of the 2014 Act.

We have not exercised any of these statutory reporting powers.

The 2014 Act also gives rights to local electors and other parties, such as the right to ask questions of the auditor and the right to make an objection to an item of account. We have not received any questions or objections that relate to the financial statements of the Derbyshire Pension Fund.

Consistency Report

We are required to provide a Consistency Report setting out whether the Pension Fund financial statements within the Pension Fund annual report are consistent with the financial statements of Derbyshire County Council. We will issue our Consistency Report once this work has been completed including our opinion that the Pension Fund financial statements are consistent with the audited financial statements of Derbyshire County Council for the year ended 31 March 2019 and comply with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2018/19. We will issue our audit certificate once this work is completed.

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

4. OUR FEES

Fees for work as the Pension Fund'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.

We have completed our work for the 2018/19 financial year, but at the time of producing this report, we have not yet finalised our audit fees for the year. If the final fee varies from that in the table below, we will write to the Director of Finance & ICT setting out the proposed variation and any reasons for the variation, and seeking agreement to it. Any variations to the final fee will also require the approval of Public Sector Audit Appointments Limited, which manages the contracts for our work.

Area of work	2018/19 proposed fee	2018/19 final fee ***
Delivery of audit work under the NAO Code of Audit Practice	£22,077 plus VAT	£22,077 plus VAT

*** Please note the final fee does not include the £16,800 detailed below which is the total chargeable by the Pension Fund to fourteen participating employers for assurances given to their auditors and that at the time of producing this report, the audit fee has not yet been finalised.

Fees for other work

In response to requests received we have reported the results of the performance of our work programme at Derbyshire Pension Fund to the auditors of fourteen participating employers. The fee for this IAS 19 assurance work is £1,200 per employer. We are satisfied this IAS 19 assurance work does not impact our independence or objectivity in relation to the audit of the Pension Fund.

In previous years we have not charged employers or their auditors for this work where the employer was within the PSAA regime and have charged employer auditors where the employer was outside of the PSAA regime. As the number of these requests is increasing year on year, from 2018/19 Mazars is charging all employers for IAS19 assurance work. The PSAA has clarified that fees for all such work, regardless of whether the employer is within the PSAA regime, will be an audit fee variation, which means that the fees for the IAS19 assurance work will be billed to the Pension Fund; the expectation is that the Fund will seek to recover the costs of this work from relevant employers.

At the present time we have not been separately engaged by the Pension Fund to carry out any other additional work outside of the fees in relation to our appointment by PSAA. Before agreeing to any other non-PSAA work we will confirm there were no actual, potential or perceived threats to our independence.

5. 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 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.

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

We will focus our work on the risks that your challenges present to your financial statements.

In the coming year we will continue to support the Pension Fund by:

- continued liaison with Internal Audit 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 management 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 Pension Fund 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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