

Annual Audit Letter

Derbyshire County Council

Year ending 31 March 2020





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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 County Council (the Council) for the year ended 31 March 2020. 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 | Assessment | Summary |
|--|--|---|
| Audit of the financial statements |  [GREEN] | Our auditor's report issued on 16 December 2020 included our opinion that the financial statements: <ul style="list-style-type: none">• give a true and fair view of the Council's financial position as at 31 March 2020 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 2019/20 |
| Other information published alongside the audited financial statements |  [GREEN] | Our auditor's report included our opinion that: <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 |  [GREEN] | 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 2020 |
| Reporting to the group auditor |  [GREEN] | In line with group audit instructions, issued by the NAO on 4 th November, we reported to the group auditor in line with the requirements applicable to the Council's Whole of Government Accounts return on 25 February 2021. |
| Statutory reporting |  [GREEN] | 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. |

Executive summary

Audit of the financial statements

Value for money conclusion

Other reporting responsibilities

Our fees

Forward look

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 2020 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 National Audit Office and International Standards on Auditing. 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, stated that in our view, the financial statements give a true and fair view of the Council's financial position as at 31 March 2020 and of its financial performance for the year then ended.

Our auditor's report was modified to include an emphasis of matters paragraph. This drew attention to the financial statement disclosure explaining that COVID-19 had contributed to 'material valuation uncertainty' in the valuation of the Council's land and buildings, and in the Council's share of Derbyshire Pension Fund's property assets included in the estimated net Pension Liability.



2. AUDIT OF THE FINANCIAL STATEMENTS

Our approach to materiality

We apply the concept of materiality when planning and performing our audit. 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. We set materiality for the financial statements as a whole (financial statement materiality) and set 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 2020:

| | | |
|---------------------------------|--|----------------------|
| Financial statement materiality | Our financial statement materiality is based on 2% of Gross Operating Expenditure. | £30,656k |
| Trivial threshold | Our trivial threshold is based on 3% of financial statement materiality. | £920k |
| Specific materiality | We have applied a lower level of materiality to the following areas of the accounts: <ul style="list-style-type: none">• Senior Officer Remuneration• Members Allowances• External Audit Fee | £5k £162k £14k |



2. AUDIT OF THE FINANCIAL STATEMENTS

Our response to significant audit 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 within 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 In all entities, 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. Because of the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits</p> | <p>We addressed this risk through performing audit testing over accounting estimates and financial journal entries and considering any significant transactions outside the normal course of business.</p> | <p>Our audit procedures did not identify any material errors or uncertainties in the financial statements, or other matters that we wish to bring to Members' attention.</p> |
| <p>Valuation of Property, Plant and Equipment The Council's accounts contain material balances relating to its Property, Plant and Equipment with the majority of these assets required to be carried at valuation.</p> | <p>We performed a range of audit tests, including, but not limited to:</p> <ul style="list-style-type: none"> • Reviewing the valuer's qualifications, objectivity and independence to carry out the required programme of revaluations. • Testing a sample of valuations to ensure the correct methodology had been applied and were supported by appropriate evidence. • Considering the impact of assets not revalued in 2019/20 to ensure these remained materially correct at the balance sheet date. | <p>The Council's valuer declared that the valuation of the Council's property assets were subject to 'material valuation uncertainty' as a result of COVID-19 and this was disclosed in Note 3 of the financial statements and referred to in the 'emphasis of matter' paragraph in our audit report. A 'material valuation uncertainty' declaration does not mean that the valuation cannot be relied upon, only that, because of the extraordinary circumstances arising from COVID-19, less certainty can be attached to the valuation.</p> |



2. AUDIT OF THE FINANCIAL STATEMENTS

Our response to significant audit risks (continued)

| Identified significant risk | Our response | Our findings and conclusions |
|--|--|---|
| <p>Valuation of the Net Pension Liability</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 <i>International Accounting Standard 19 Employee Benefits</i>.</p> | <p>We performed a range of audit tests, including, but not limited to:</p> <ul style="list-style-type: none"> • Liaising with the auditor of the Derbyshire Pension Fund to obtain direct assurance over the controls surrounding membership, contributions and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements. • 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. • Considered the impact of the remedy solution for the McCloud legal judgement on the net pension liability. | <p>'Material valuation uncertainty' was disclosed on the Pension Fund's property investment assets as a result of COVID-19. As the Council's share of those assets in the net Pension Liability in its own balance sheet is material, the Council has disclosed this in Note 3 of the financial statements and we have reflected this in the 'emphasis of matters' paragraph in our Audit Report.</p> |
| <p>Revenue Recognition</p> <p>Under <i>International Standards on Auditing 240</i>, there is a presumed risk that revenue may be misstated due to improper revenue recognition.</p> | <p>We evaluated the design and implementation of controls to mitigate the risk of material debtors being recognised in the wrong period. We tested debtors to ensure that they are supported by sufficient and appropriate evidence and were accounted for correctly.</p> <p>Our audit approach also incorporated a range of other substantive procedures, including, but not limited to the testing of receipts around the year-end to provide assurance that any material items of income had been recorded in the correct financial year</p> | <p>Our audit procedures in relation to this risk did not identify any material errors or uncertainties in the financial statements, or other matters that we wish to bring to your attention.</p> |



2. AUDIT OF THE FINANCIAL STATEMENTS

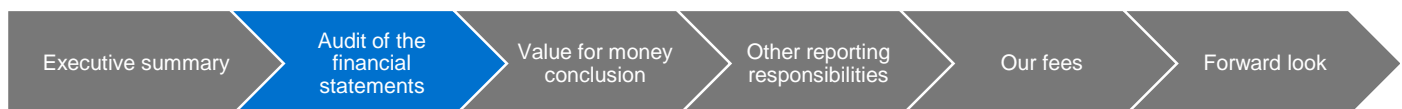
Our response to areas of management judgement

| Identified management judgement | Our response | Our findings and conclusions |
|---|---|--|
| <p>Minimum Revenue Provision (MRP) Local authorities are required each year to set aside some of their revenues as provision for debt in respect of capital expenditure financed by borrowing or long term credit arrangements. The amount to be set aside each year is not prescribed, although an overarching principle of prudence is expected to be adopted. This is supported by statutory guidance as to how this could be achieved and the Council is required to have regard to this in setting its MRP policy. Management judgement is therefore exercised in determining the level of its prudent provision.</p> | <p>We addressed this judgement by:</p> <ul style="list-style-type: none"> • reviewing the Council’s MRP policy to ensure that it continues to have been developed with regard to the statutory guidance; • assessing whether the provision had been calculated and recorded in accordance with the Council's policy; and • assessing whether the amount provided for the period is appropriate, taking into account the Council's Capital Financing Requirement. | <p>Our audit procedures did not identify any material errors or uncertainties in the 2019/20 financial statements in relation to the Council’s MRP</p> |
| <p>SinFin Waste Recycling The long-term waste management contract between Derbyshire County Council, Derby City Council and Resource Recovery Solutions came to an end in 2019. The Council’s management had to make a judgement on how to account for the impact in 2019/20.</p> | <p>We evaluated the basis of the accounting judgement and the impact on the financial statements for 2019/20 including the adequacy of the related disclosures.</p> | <p>The procedures we have undertaken did not identify any material errors or uncertainties in the financial statements, or other matters to bring to Members’ attention.</p> |

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. The matters we report are limited to those deficiencies and other control recommendations that we have identified during our normal audit procedures and that we consider to be of sufficient importance to merit being reported.

We reported a small number of minor control deficiencies in our Audit Completion Report presented to the Audit Committee in November 2020.



3. VALUE FOR MONEY CONCLUSION

Value for money conclusion

Unqualified

Our audit approach

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.

Significant audit risks

The NAO’s guidance requires us to carry out work to identify whether or not a risk to our conclusion exists. Risk, in the context of our 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.

When we perform our work, we consider whether there are any areas requiring additional audit attention as a “Significant Audit Risk”, which we report to the Audit Committee prior to finalising our conclusion. For 2019/20, we identified one significant audit risk:

- SinFin Waste Recycling – The long-term waste management contract between Derbyshire County Council, Derby City Council and Resource Recovery Solutions that came to an end in 2019.

Findings

The facility was due to be operational in 2017, however this did not happen as intended. Following a sustained period of the Councils asking the funding banks to step-in and get the Waste Recycling facility fully operational, the banks issued a legal notice (called a “No Liquid Market” notice) that brought the contract to an end and the councils did not dispute the notice.

We reviewed the governance and decision making in respect of this project before offering our 2019/20 VFM conclusion. In undertaking this work we considered the timeline of key decisions made by the Council and the reports issued in support of those decisions.

Overall, we obtained sufficient assurance to conclude that the Council has appropriate arrangements in place.

Overall Conclusion

Our auditor’s report stated that 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 2020.



4. OTHER REPORTING RESPONSIBILITIES

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

The 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 did not receive any such objections or questions.

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

The National Audit Office, as group auditor, requires us to complete a Whole of Government Accounts Assurance Statement in respect of financial consolidation data produced by the Council. We submitted this information to the NAO on 25 February 2021.

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 in March 2020 as £39,307, plus amounts to be confirmed to cover the additional testing on Property, Plant & Equipment and Defined Benefit Pensions Schemes.

Having completed our work for the 2019/20 financial year, we can confirm that our final fees are as follows:

| Area of work | 2019/20 proposed fee | 2019/20 Final fee |
|---|----------------------|-------------------|
| Delivery of audit work under the NAO Code of Audit Practice | £96,524 | |
| Fee Variations*: | | |
| • Additional Testing on Property, Plant & Equipment and Defined Benefit Pensions Schemes | | £8,230 |
| • Additional Costs associated with being a 'Major Local Audit' and requiring additional level of audit procedures and quality control | | £3,735 |
| • Additional costs associated with 2019/20, including, but not limited to: | | £6,145 |
| • Impact of 'Material Valuation Uncertainty' in Council's Property Assets and its share of Pension Fund Assets | | |
| • Updating audit risk assessments, including the value for money conclusion | | |
| • Additional considerations of estimation uncertainty and the Going Concern assertion | | |
| • Changes impacting pension liabilities through McCloud and Goodwin | | |
| Final audit fee | | £114,634 |
| Other non-Code work | | |
| • Assurance on the Teachers Pensions Return | £3,700 | £3,700 |

*Fee variations subject to confirmation from PSAA.

Fees for other work

We confirm that we have not undertaken any non-audit services for the Council in the year.



6. FORWARD LOOK: AUDIT CHANGES 2020/21

Changes to the Code of Audit Practice

The Code of Audit Practice (the Audit Code), issued by the Comptroller and Auditor General, prescribes the way we carry out our responsibilities as your auditors. On 1st April 2020 a new Code came in to force and will apply to our work from 2020/21 onwards.

The new Audit Code continues to apply the requirements of International Standards on Auditing (ISAs) to our audit of the financial statements. While there are changes to the ISAs that are effective from 2020/21 the Audit Code has not introduced any changes to the scope of our audit of the financial statements. We will continue to give our opinion on the financial statements in our independent auditor's report.

There are however significant changes to the work on value for money arrangements, and the way we report the outcomes of our work to you.

The auditor's work on value for money arrangements

From 2020/21 we are still required to satisfy ourselves that you have made proper arrangements for securing the economy, efficiency and effectiveness in your use of resources, however unlike under the 2015 Audit Code, we will no longer report in the form of a conclusion on arrangements. Instead, where our work identifies significant weaknesses in arrangements, we are required to report those weaknesses to you, along with the actions that need to be taken to address those weaknesses.

Our work will focus on three criteria specified in the revised Audit Code:

- Financial sustainability: how the body plans and manages its resources to ensure it can continue to deliver its services;
- Governance: how the body ensures that it makes informed decisions and properly manages its risks; and
- Improving economy, efficiency and effectiveness: how the body uses information about its costs and performance to improve the way it manages and delivers its services.

Under the new Audit Code, we will be expected to report and make recommendations as soon as we identify a significant weakness in arrangements, as opposed to reporting our conclusion on arrangements at the end of the audit cycle as has previously been the case.

Reporting the results of the auditor's work

We currently issue you with an Annual Audit Letter which provides a summary of our work across all aspects of our audit. From 2020/21 the Annual Audit Letter will be replaced by the Auditor's Annual Report. This will continue to provide a summary of our work over the year of audit but will also include a detailed commentary on your arrangements in place to achieve economy, efficiency and effectiveness. This commentary replaces the conclusion on arrangements that was previously provided and will include details of any significant weakness identified and reported to you, follow up of any previous recommendations made, and our view as to whether recommendations have been implemented satisfactorily.

The new Audit Code will result in additional officer time and auditor time and therefore audit fees.



6. FORWARD LOOK: AUDIT CHANGES 2020/21

Redmond Review

In September 2020, Sir Tony Redmond published the findings of his independent review into the oversight of local audit and the transparency of local authority financial reporting. The report makes several recommendations that, if implemented, could affect both the financial statements that local authorities are required to prepare and the work that we as auditors are required to do.

The report and recommendations are wide-ranging, and includes:

- the creation of the Office of Local Audit and Regulation (OLAR), to manage, oversee and regulate local audit;
- reviewing reporting deadlines;
- reviewing governance arrangements in local authorities, including the membership of the Governance, Audit & Standards Committee; and
- increasing transparency and reducing the complexity of local authority financial statements.

The recommendations and findings will now be considered by the Ministry of Housing, Communities and Local Government and we look forward to working with all stakeholders to implement changes to ensure the development and sustainability of local audit.

The full report is available here: <https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-independent-review>

The recommendations and findings have been considered by the Ministry of Housing, Communities and Local Government and a response was published in December 2020

<https://www.gov.uk/government/publications/local-authority-financial-reporting-and-external-audit-government-response-to-the-redmond-review/local-authority-financial-reporting-and-external-audit-government-response-to-the-independent-review>

The main highlights are a recognition that fees are not sufficient to meet the work required, and the date for publication of audited accounts has been confirmed as 30th September for the 20/21 and 21/22 financial years (with a commitment to review whether it is realistic to return to a 31st July date)

A new body to oversee local audit will not be created, however, a new, audited 'standardised statement of service information and costs' to be produced by LG bodies, with CIPFA being asked to work on this for introduction in 2021/22.



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