

The Annual Audit Letter for North Somerset Council

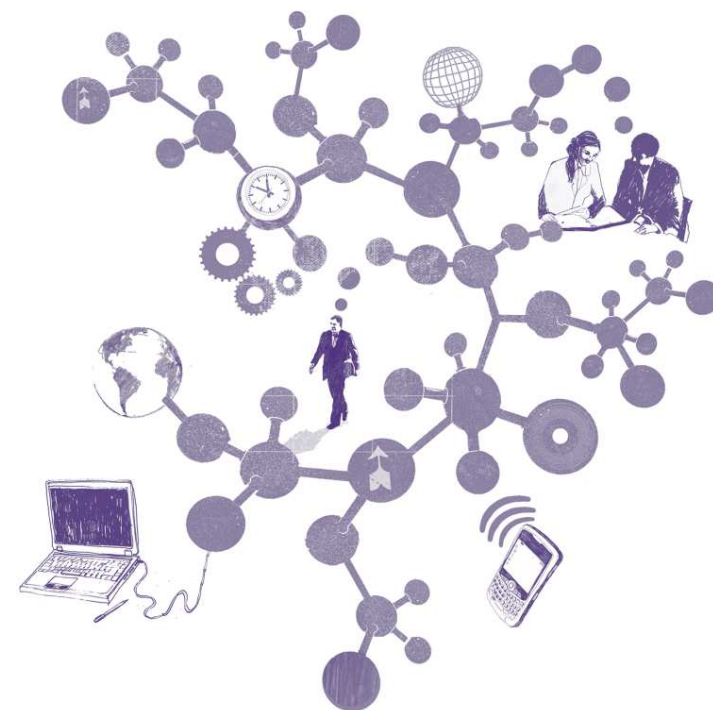
Year ended 31 March 2016

21 October 2016

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Executive summary

Purpose of this letter

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at North Somerset Council (the Council) for the year ended 31 March 2016.

This Letter is intended to provide a commentary on the results of our work to the Council and its external stakeholders, and to highlight issues that we wish to draw to the attention of the public. In preparing this letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice (the Code) and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'.

We reported the detailed findings from our audit work to the Council's Audit Committee as those charged with governance in our Audit Findings Report on 7th September 2016.

Our responsibilities

We have carried out our audit in accordance with the NAO's Code, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

- give an opinion on the Council's financial statements (section two)
- assess the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money conclusion) (section three).

In our audit of the Council's financial statements, we comply with International Standards on Auditing (UK and Ireland) (ISAs) and other guidance issued by the NAO.

Our work

Financial statements opinion

We gave an unqualified opinion on the Council's financial statements on 28 September 2016.

Value for money conclusion

We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2016. We reflected this in our audit opinion on 28 September 2016.

Whole of government accounts

We completed work on the Council's consolidation return following guidance issued by the NAO and issued an unqualified report on 28 September 2016.

Certificate

We certified that we had completed the audit of the accounts of North Somerset Council in accordance with the requirements of the Code on 28 September 2016.

Certification of grants

We also carry out work to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. Our work on this claim is not yet complete and will be finalised by 30 November 2016. We will report the results of this work to the Audit Committee in our Annual Certification Letter.

Working with the Council

During the year we have delivered a number of successful outcomes with you:

- An efficient audit – we delivered the accounts in line with the timescale we agreed with you.
- Sharing our insight – through regular Audit Committee Updates.
- Thought leadership – through the sharing of our publications and workshops
- Provide training – through the provision of technical workshops
- Providing information – through, for example, providing information from our CFO Insights tool.

We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Council's staff.

Grant Thornton UK LLP
October 2016

Audit of the accounts

Our audit approach

Materiality

In our audit of the Council's accounts, we use the concept of materiality to determine the nature, timing and extent of our work, and in evaluating the results of our work. We define materiality as the size of the misstatement in the financial statements that would lead a reasonably knowledgeable person to change or influence their economic decisions.

We determined materiality for our audit of the Council's accounts to be £8,900,000, which is 2% of the Council's gross revenue expenditure. We used this benchmark, as in our view, users of the Council's accounts are most interested in how it has spent the income it has raised from taxation and grants during the year.

We also set a lower level of specific materiality for certain areas such as the disclosures of officers' remuneration, salary bandings, exit packages, members allowances and auditors remuneration in notes to the statements due to the public interest in these disclosures and the statutory requirement for them to be made. We set a lower threshold of £5,000, above which we reported errors to the Audit Committee in our Audit Findings Report.

The scope of our audit

Our audit involves obtaining enough evidence about the amounts and disclosures in the financial statements to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error.

This includes assessing whether:

- the Council's accounting policies are appropriate, have been consistently applied and adequately disclosed;
- significant accounting estimates made by management are reasonable; and
- the overall presentation of the financial statements gives a true and fair view.

We also read the Narrative Report and Annual Governance Statement to check they are consistent with our understanding of the Council and with the accounts on which we give our opinion.

We carry out our audit in line with ISAs (UK and Ireland) and the NAO Code. We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach was based on a thorough understanding of the Council's business and is risk based.

We identified key risks and set out overleaf the work we performed in response to these risks and the results of this work.

Audit of the accounts

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk
<p>The revenue cycle includes fraudulent transactions</p> <p>Under ISA (UK&I) 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.</p>	<p>Having considered the risk factors set out in ISA240 and the nature of the revenue streams at North Somerset Council, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because:</p> <ul style="list-style-type: none">• there is little incentive to manipulate revenue recognition• opportunities to manipulate revenue recognition are very limited; and• the culture and ethical frameworks of local authorities, including North Somerset Council, mean that all forms of fraud are seen as unacceptable.
<p>Management over-ride of controls</p> <p>Under ISA (UK&I) 240 it is presumed that the risk of management over-ride of controls is present in all entities.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none">• Reviewed accounting estimates, judgements and decisions made by management• Tested journal entries• Reviewed unusual significant transactions• Reviewed assurances from the Audit Committee and management in relation to fraud, law and regulations• Reviewed accounting estimates, judgements and decisions made by management• Tested journal entries• Reviewed unusual significant transactions

Audit of the accounts

These are the risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk
<p>Valuation of property, plant and equipment and Investment property</p> <p>The Council revalues its PPE assets on a rolling basis with assets revalued at least every five years . The Code requires that the Council ensures that the carrying value at the balance sheet date is not materially different from current value. This represents a significant estimate by management in the financial statements.</p> <p>The CIPFA Code of Practice has implemented IFRS 13 for the 2015/16 financial statements. The Council is required to include Investment property in its financial statements at fair value, as defined by IFRS13. The basis on which fair value is defined for investment property is different to that used in previous years.</p> <p>This represents a significant change in the basis for estimation of these balances in the financial statements.</p> <p>There are also extensive disclosure requirements under IFRS 13 which the Council needs to comply with.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • Reviewed management's processes and assumptions for the calculation of related estimates. • Identified the controls put in place by management to ensure that the carrying values of property, plant and equipment, and investment property, were not materially different from fair value at the year end. We also assessed whether these controls were implemented as expected, and whether they were sufficient to mitigate the risk of material mis-statement. • Reviewed the competence, expertise and objectivity of any management experts used. • Reviewed the instructions issued to valuation experts and the scope of their work • Held discussions with the Council's valuer about the basis on which the valuation was carried out, challenging the key assumptions. • Reviewed and challenged the information used by the valuer to ensure it was robust and consistent with our understanding. • Reviewed and challenged the reasonableness of the proposed revaluations, including reference to national trends • Tested revaluations made during the year to ensure they were input correctly into the Council's asset register • Evaluated the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value. • Reviewed the disclosures made by the Council in its financial statements to ensure they are in accordance with the requirements of the CIPFA Code of Practice and IFRS 13. • Reviewed Investment properties to ensure that they were all revalued during the year <p>We did not identify any issues to report</p>

Audit of the accounts (continued)

Risks identified in our audit plan	How we responded to the risk
<p>Valuation of pension fund net liability</p> <p>The Council's pension fund asset and liability as reflected in its balance sheet represent significant estimates in the financial statements.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • Documented the key controls that were put in place by management to ensure that the pension fund liability was not materially misstated. • Completed a walkthrough of the key controls to assess whether they were implemented as expected and mitigate the risk of material misstatement in the financial statements. • Reviewed the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation. We will gain an understanding of the basis on which the valuation is carried out. • Undertook procedures to confirm the reasonableness of the actuarial assumptions made. • Gained an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made. • Reviewed the consistency of the pension fund asset and liability and disclosures in notes to the financial statements with the actuarial report from your actuary. <p>We did not identify any issues to report</p>
<p>Accounting for the Better Care Fund (BCF)</p> <p>The accounts are due to include new, material pooled budget disclosure, and underlying transactions re BCF. Judgement is required in assessing the required accounting treatment.</p> <p>Risks identified include:</p> <ul style="list-style-type: none"> • Has the Council entered into appropriate arrangements to account for BCF monies? • Does the Council have appropriate processes in place to obtain the information it needs to reflect the correct transactions, balances and disclosures in its accounts? • Are the judgements made by the Council in assessing its control over the funds reasonable, and hence has it adopted the correct accounting treatment in the accounts? • Do BCF transactions, balances, and disclosures in the accounts agree to underlying evidence? 	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • Identified the controls put in place by management to ensure that the BCF accounting entries and disclosures were not materially misstated. We assessed whether these controls were implemented as expected, and whether they were sufficient to mitigate the risk of material misstatement. • Reviewed to ensure signed s75 agreements in place for all BCF transactions covered by pooled budget accounting. • Reviewed the Council's processes for obtaining the information it needs to reflect the correct transactions, balances and disclosures in its accounts. • Reviewed the reasonableness of the Council's judgements in assessing the Council's control over the funds, and hence adopted the correct accounting treatment in the accounts • Reviewed to ensure that BCF transactions, balances, and disclosures in the accounts agree to underlying evidence. <p>We did not identify any issues to report</p>

Audit of the accounts

Audit opinion

We gave an unqualified opinion on the Council's accounts on 28 September 2016, in advance of the 30 September 2016 national deadline.

The Council made the accounts available for audit in line with the agreed timetable, and provided good quality working papers to support them, although we noted more errors than in recent years. The finance team responded promptly and efficiently to our queries during the course of the audit.

Issues arising from the audit of the accounts

We reported the key issues from our audit of the accounts of the Council to the Council's Audit Committee on 7 September 2016.

Annual Governance Statement and Narrative Report

We are also required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website with the draft accounts in line with the national deadlines.

Whole of Government Accounts (WGA)

We carried out work on the Council's consolidation schedule in line with instructions provided by the NAO . We issued a group assurance certificate which did not identify any issues for the group auditor to consider.

Other statutory duties

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the Council's accounts and to raise objections received in relation to the accounts. We have not identified any issues that have required us to apply our statutory powers and duties under the Act.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code (the Code), following the guidance issued by the NAO in November 2015 which specified the criterion for auditors to evaluate:

In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the key risks where we concentrated our work.

The key risk we identified and the work we performed are set out overleaf.

As part of our Audit Findings report agreed with the Council in September 2016, we raised the following recommendations to address our findings.

1. that the FSB and CMT continue to receive budget monitoring reports and appropriately challenge the officers
2. Members should continue to receive training on how to challenge officers and that evidencing of this challenge is improved and strengthened.
3. Members of the Adult Scrutiny Panel should be made aware of their duties and fully comply with the requirements of the Constitution.
4. the Council consider providing training for those involved in the budget setting process to ensure that they understand the importance of setting realistic budgets

Overall VfM conclusion

We are satisfied 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 ending 31 March 2016.

Value for Money

Value for money risks

Risk identified	Work carried out	Findings and conclusions
<p>Strategic Financial Planning</p> <p>In February 2016 the Council revised its Medium Term Financial Plan (MTFP) in light of the settlement figure announced on 17 December 2015 as this left the Council with an increased funding gap. The revised MTFP highlights a balanced budget for 2016/17, but a savings target of £8.6 million. In addition, the Council have updated the Corporate Plan to sit alongside the revised MTFP and highlights numerous projects and initiatives the Council wish to undertake. The Council therefore continues to face challenges in securing the funding, achieving the savings and delivering a balanced budget.</p>	<p>We reviewed the Councils progress on delivering the 2015/16 savings plan and the extent to which 2016/17 savings plan is achievable. We also reviewed the assumptions behind the MTFP and the work that the Council is doing to close the funding gap.</p>	<p>The Council delivered £14 million out of the £15.5 million savings planned for 2015/16. This shows a strong performance considering that this is not the first year that the Council has been required to make savings. The remaining £1.5 million will be rolled forward into future saving plans. At 31 March 2016, there was an overspend by the Council against its final budget. Larger overspends in Children's and Young People and Adult Social Care were offset by underspends in other Directorates and the use of Contingency Budgets resulting in approximately an £800k overspend in total.</p> <p>The Council recognises that there are significant pressures on delivering the £8.5 million savings plan for 2016/17, mainly due to significant increases in the cost and volume of Learning Disabled clients and delays in implementing some of the planned mitigations. The 2016/17 savings plan is therefore being monitored by the Financial Strategy Board (FSB) and the Corporate Management Team (CMT) and both of these groups receive monthly monitoring against budgets. We would therefore recommend that the FSB and CMT continue to receive budget monitoring reports and appropriately challenge the officers. From reviewing the public minutes, there appears to be no challenge of Officers regarding the month 12 overspend at the Scrutiny Panels, Executive or Full Council meetings. Officers have confirmed that challenge was provided by members, however this does not appear to be recorded in the minutes. Members should therefore continue to scrutinise. We would therefore recommend that the Members should continue to receive training on how to challenge officers and that evidencing of this challenge is improved and strengthened. As part of our review over the public records, we noted that the Adult Scrutiny Panel has not taken an Annual Report to Full Council since January 2015. This is in breach of the Constitution, which states that Scrutiny Panels should take an Annual Report at least once a year. We would therefore recommend that members of the Adult Scrutiny Panel be made aware of their duties and fully comply with the requirements of the Constitution.</p>

Value for Money (continued)

Value for money risks (continued)

Risk identified	Work carried out	Findings and conclusions
		<p>The assumptions behind the MTFP appear to be reasonable, with the Council moving to a Cost and Volume basis where applicable. This data, whilst estimated initially based on past experience, will become more robust as the data is updated each quarter and patterns and trends can be determined. We do have concerns over the robustness of some of the data, particularly within Adult Social Care and Children's Services as initial actual data appears to be showing significant variances against budget. We would therefore recommend that the Council consider providing training for those involved in the budget setting process to ensure that they understand the importance of setting realistic budgets.</p> <p>The current MTFP still has a gap in future years. We have noted that the Head of Finance and Property and his team are working on proposals to close the future funding gap, which are currently in initial stages. Feasibility work is being undertaken on proposals to determine which options are viable and will deliver the savings that the Council needs. All Directorates are involved in the process and this is being overseen by the CMT.</p> <p>We have also noted that where appropriate, costs have been included within the budgets for items included within the Corporate Plan.</p> <p>Our overall conclusion on strategic financial planning is positive and is consistent with that of the draft Corporate Peer Challenge Report, which will be published by the Council in the near future.</p> <p>On that basis we concluded that the risk was sufficiently mitigated and the Council has proper arrangements</p>

Working with the Council

Our work with you in 2015/16

We are really pleased to have worked with you over the past year. We have established a positive and constructive relationship. Together we have delivered some great outcomes.

An efficient audit – we delivered the accounts in line with the timescale we agreed with you. Our audit team are knowledgeable and experienced in your financial accounts and systems. Our relationship with your team provides you with a financial statements audit that is challenging but fair.

Sharing our insight – we provided regular Audit Committee updates covering best practice. Areas we covered included 'Knowing the Ropes – Audit Committee Effectiveness Review', 'Making devolution work' and 'Reforging local government'. We have also shared with you our insights on advanced closure of local authority accounts, in our publication 'Transforming the financial reporting of local authority accounts'.

Thought leadership – We have shared with you our publication on 'Building a successful joint venture' and will continue to support you as you consider greater use of alternative delivery models for your services.

Providing training – we provided your team with training on financial accounts and annual reporting. The courses were attended by your Corporate Accountancy Manager.

Providing information – We provided you with access to CFO insights, our online analysis tool providing you with access to insight on the financial performance, socio-economy context and service outcomes of councils across the country.

Working with the Council

Working with you in 2016/17

Highways Network Asset

The Code of Practice on Local Authority Accounting (the Code) requires authorities to account for Highways Network Asset (HNA) at depreciated replacement cost (DRC) from 1 April 2016. The Code sets out the key principles but also requires compliance with the requirements of the recently published Code of Practice on the Highways Network Asset (the HNA Code), which defines the assets or components that will comprise the HNA. This includes roads, footways, structures such as bridges, street lighting, street furniture and associated land. These assets should always have been recognised within Infrastructure Assets.

The Code includes transitional arrangements for the change in asset classification and the basis of measurement from depreciated historic cost (DHC) to DRC under which these assets will be separated from other infrastructure assets, which will continue to be measured at DHC.

This is expected to have a significant impact on the Council's 2016/17 accounts, both in values and levels of disclosure, and may require considerable work to establish the opening inventory and condition of the HNA as at 1 April 2016.

Under the current basis of accounting values will only have been recorded against individual assets or components acquired after the inception of capital accounting for infrastructure assets by local authorities. Authorities may therefore have to develop new accounting records to support the change in classification and valuation of the HNA.

The nature of these changes means that Finance officers will need to work closely with colleagues in the highways department and potentially also to engage other specialists to support this work.

Some of the calculations are likely to be complex and will involve the use of external models, a combination of national and locally generated rates and a number of significant estimates and assumptions.

We have been working with the Council on the accounting, financial reporting and audit assurance implications arising from these changes. We have issued two Client Briefings which we have shared with your Corporate Accountancy Manager. We will issue further briefings during the coming year to update the Council on key developments and emerging issues.

This important accounting development is likely to be a significant risk for our 2016/17 audit, so we have already had some preliminary discussions with the Council to assess the progress it is making in this respect.

We will continue to liaise closely with the senior finance team during 2016/17 on this important accounting development, with timely feedback on any emerging issues.

The audit risks associated with this new development and the work we plan to carry out to address them will be reflected in our 2016/17 audit plan.

Working with the Council

We will also continue to work with you and support you over the next financial year with the following areas. Locally our focus will be on:

- An efficient audit – continuing to deliver an efficient audit
- Supporting development – we are in discussion with you on the faster close of the accounts preparation and will continue to liaise with relevant officers throughout the process
- Support outside of the audit – our advisory team are in discussion with you on Joint Ventures

Appendix A: Reports issued and fees

We confirm below our final fees charged for the audit and provision of non-audit services.

Fees

	Planned £	Actual fees £	2014/15 fees £
Statutory audit of Council	111,975	111,975	149,300
Housing Benefit Grant Certification	13,962	*13,962	19,560
Total fees (excluding VAT)	125,947	125,947	168,860

* Work in this area is currently in progress. Any proposed changes in fee will be discussed with the Council and are subject to approval by Public Sector Audit Appointments Ltd. The final certification fee will be reported in the Annual Certification Letter.

Reports issued

Report	Date issued
Audit Plan	March 2016
Audit Findings Report	September 2016
Annual Audit Letter	October 2016

Fees for other services

Service	Fees £
Audit related services:	
• Grant certification	
- Teachers Pensions Return	4,200
- Transport Grant	4,200
Audit related services (excluding VAT)	8,400



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