

# The Audit Findings for Newcastle under Lyme Borough Council

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**Year ended 31 March 2019**

**July 2019**



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The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed for the purpose of expressing our opinion on the financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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# Headlines

This table summarises the key findings and other matters arising from the statutory audit of Newcastle under Lyme Borough Council ('the Council') and the preparation of the Council's financial statements for the year ended 31 March 2019 for those charged with governance.

<b>Financial Statements</b>	<p>Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Council's financial statements:</p> <ul style="list-style-type: none"> <li>• give a true and fair view of the financial position of the Council income and expenditure for the year; and</li> <li>• have been properly prepared in accordance with the CIPFA/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014.</li> </ul> <p>We are also required to report whether other information published together with the audited financial statements (including the Annual Governance Statement (AGS) and Narrative Report), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</p> <p>Our audit work remains ongoing, having commenced on-site in June 2019. Our findings are summarised on pages 3 to 18. Audit adjustments are detailed in Appendix A. The financial statements included some significant errors this year and the working papers presented at audit were not all produced to the necessary standard.</p>	<p>We recognise that this was a difficult year with the retirement of a key finance officer, who has historically managed the financial closedown process, some issues outside of the Council's control and an deeper external audit focus in key areas compared to previous years.</p> <p>As a result, our work remains ongoing and will not be complete by the end of July 2019. We will not therefore be issuing an opinion on the Council's financial statements including the value for money opinion by the 31<sup>st</sup> July deadline. We have agreed with management that we will seek to conclude our on-site work during the first two weeks of August 2019, on the assumption that our work identifies no further errors and other outstanding issues are addressed. The key issues that remain to be addressed include:</p> <ul style="list-style-type: none"> <li>• Accounting treatment of Castle House</li> <li>• Valuation of the Council's former offices</li> <li>• Re-valuation of 38 assets</li> <li>• Valuation of Jubilee 2 Leisure Centre.</li> <li>• The timing of valuations carried out</li> <li>• Resolution of Pension Accounting issues.</li> </ul> <p>In addition to the above, significant areas of testing remain in progress across the audit. Significant audit findings based on work to date are included in the Action Plan at Appendix A.</p>
<b>Value for Money arrangements</b>	<p>Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report if, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion').</p>	<p>Our risk based review of the Council's value for money arrangements, remains in progress.</p> <p>Our findings, based on the work to date are summarised on pages 14 to 18.</p>
<b>Statutory duties</b>	<p>The Local Audit and Accountability Act 2014 ('the Act') also requires us to:</p> <ul style="list-style-type: none"> <li>• report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and</li> <li>• To certify the closure of the audit.</li> </ul>	<p>We have not exercised any of our additional statutory powers or duties in respect to the 2018/19 financial year.</p> <p>Our audit work remains ongoing under the Code and we expect to be able to certify the completion of the audit when we give our audit opinion.</p>

## Acknowledgements

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

# Summary

## Overview of the scope of our audit

This Audit Findings Report presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management.

As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK) and the Code, which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

## Audit approach

Our audit approach was based on a thorough understanding of the Council's business and is risk based, and in particular included:

- An evaluation of the Council's internal controls environment, including its IT systems and controls; and
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks

We have not had to alter or change our audit plan, as communicated to you in January 2019.

## Conclusion

Our work remains ongoing and will not be completed by the end of July 2019. Therefore, we will not be issuing an opinion on the Council's financial statements including the value for money opinion by the 31<sup>st</sup> July deadline. We have agreed with management that we will seek to conclude our on-site work during the first two weeks of August 2019.

The key issues that remain to be addressed include:

- Accounting treatment of Castle House
- Valuation of the Council's former offices
- Valuation of Jubilee 2 Leisure Centre.
- Revaluation of 38 assets
- The timing of valuations carried out
- Resolution of Pension Accounting issues.

In addition to the above, significant areas of testing remain to be completed across the audit.

Following conclusion of our audit work, we will be required to report our findings to the Council prior to the approval of the financial statements and the letter of representation. The Council needs to determine whether this needs to be done through another formal Audit Committee or whether it can do through delegated arrangements.

We would remind the Council that they are still required to publish their financial statements by the 31<sup>st</sup> July 2019 deadline. The Council would still be in compliance with the Accounts and Audit Regulations 2015 if they publish an explanation of why audited accounts are not available by 31 July 2019.

## Our approach to materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law. Materiality calculations remain the same as reported in our Audit Plan.

### Council Amount (£) Qualitative factors considered

Materiality for the financial statements	1,250,000	Based on a proportion of forecast gross expenditure (2%) for the financial year. In the prior year we used the same benchmark.
Performance materiality	875,000	Quality of financial systems and processes and the nature of the Council's income and expenditure streams. Quality of accounts and working papers in previous years and level of amendments arising from audit process.
Trivial matters	62,000	Set at 5% of materiality.
Materiality for specific transactions, balances or disclosures	100,000	Lower materiality applied to remuneration disclosures due to their sensitive nature and public interest.

# Significant findings – audit risks

Risks identified in our Audit Plan	Commentary
<p><b>1 The revenue cycle includes fraudulent transactions</b></p> <p>Under ISA (UK) 240 there is a rebuttable 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><b>Auditor commentary</b></p> <p>Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Council, we determined that the risk of fraud arising from revenue recognition could be rebutted, because:</p> <ul style="list-style-type: none"> <li>• there is little incentive to manipulate revenue recognition.</li> <li>• opportunities to manipulate revenue recognition are very limited.</li> <li>• the culture and ethical frameworks of local authorities, including Newcastle under Lyme Borough Council, mean that all forms of fraud are seen as unacceptable.</li> </ul> <p>Therefore we did not consider this to be a significant risk for Newcastle under Lyme Borough Council.</p> <p>There were no changes to our assessment as reported in the audit plan that we need to bring to your attention.</p> <p>Whilst not a significant risk, as part of our audit work we are undertaking work on material revenue items. Our work to date has not identified any matters that would indicate our rebuttal was incorrect.</p>
<p><b>2 Management override of controls</b></p> <p>Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities.</p> <p>Management over-ride of controls is a risk requiring special audit consideration.</p>	<p><b>Auditor commentary</b></p> <p>We have:</p> <ul style="list-style-type: none"> <li>• evaluated the design effectiveness of management controls over journals</li> <li>• analysed the journals listing and determine the criteria for selecting high risk unusual journals</li> <li>• tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration</li> <li>• gained an understanding of the accounting estimates, critical judgements applied and decisions made by management and consider their reasonableness with regard to corroborative evidence</li> <li>• evaluated the rationale for any changes in accounting policies or significant unusual transactions.</li> </ul> <p>Based on the work to date, our audit work has not identified any issues in respect of management override of controls.</p>

# Significant findings – audit risks

Risks identified in our Audit Plan	Commentary
<p><b>3 Valuation of property, plant and equipment (land and buildings)</b></p> <p>The Authority revalue's its land and buildings on a rolling five-yearly basis. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the Authority financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date, where a rolling programme is used.</p> <p>W therefore identified the valuation of land and buildings, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p><b>Auditor commentary</b></p> <p>We have:</p> <ul style="list-style-type: none"> <li>evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to the valuations experts and the scope of their work;</li> <li>evaluated the competence, capabilities and objectivity of the valuation expert;</li> <li>Contacted the valuer to confirm the basis on which the valuation was carried out to ensure that the requirements of the CIPFA code were met;</li> <li>challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding;</li> <li>tested revaluations made during the year to see if they had been input correctly into the Authority's asset register and accounted for correctly; and</li> <li>evaluated the assumptions made by management for those assets not revalued during the year, as well as any assets revalued during the year but prior to year end, and how management have satisfied themselves that these are not materially different to current value at year end.</li> </ul> <p>Our audit work has identified a number of issues in respect of valuation of land and buildings. These are set out page 8 under Significant Findings – Other Issues.</p>

# Significant findings – audit risks

Risks identified in our Audit Plan	Commentary
<p><b>4 Valuation of pension fund net liability</b></p> <p>The Authority's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements.</p> <p>The pension fund net liability is considered a significant estimate due to the size of the numbers involved and the sensitivity of the estimate to changes in key assumptions.</p> <p>We therefore identified the valuation of the Authority's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p><b>Auditor commentary</b></p> <p><b>We have</b></p> <ul style="list-style-type: none"> <li>• updated our understanding of the processes and controls put in place by management to ensure that the Authority's net pension fund liability is not materially misstated and evaluated the design of the associated controls;</li> <li>• evaluated the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work;</li> <li>• assessed the competence, capabilities and objectivity of the actuary who carried out the Authority's pension fund valuation;</li> <li>• assessed the accuracy and completeness of the information provided by the Authority to the actuary to estimate the liability;</li> <li>• tested the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary;</li> <li>• undertaken procedures to confirm the reasonableness of the actuarial assumptions using the report of a consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report; and</li> <li>• Obtained assurances from the auditor of the Staffordshire Pension Fund to the controls surrounding the validity and accuracy of membership data, contributions data and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements.</li> </ul> <p><b>Impact of the McCloud judgement</b></p> <p>The Court of Appeal has ruled that there was age discrimination in the judges and firefighters pension schemes where transitional protections were given to scheme members. The legal ruling around age discrimination (McCloud - Court of Appeal) has implications not just for pension funds, but also for other pension schemes where they have implemented transitional arrangements on changing benefits. The LGPS Scheme Advisory Board (with the consent of the Ministry of Housing, Communities and Local Government) commissioned GAD to prepare an assessment of the financial impact of the McCloud judgement on an LGPS scheme-wide basis to inform the financial reporting of participating entities. The report shows the estimates of the cost of the remedy if the LGPS underpin was found to result in unlawful age discrimination.</p> <p>As a result of the ruling we have worked with the Authority to consider the implications and as a result the Authority commissioned a further actuarial assessment to include the impact of the case. This resulted in an increase in the net pensions liability recorded in the Authority's accounts, with the liability increasing by £2.330 million, as a result of McCloud £554k, GMP equalisation £387k and impact of actual asset returns £1,389k. We have carried out additional work locally and nationally to assess the approach and assumptions used by the actuary in providing this updated estimate.</p> <p><b>Conclusion</b></p> <p>The Authority proposes to adjust its pensions liability in its financial statements to incorporate the estimated impact of the McCloud judgement. Our audit procedures will confirm that the updated estimate is reasonable.</p>



# Significant findings - other issues

This section provides commentary on new issues and risks which were identified during the course of the audit that were not previously communicated in the Audit Plan and a summary of any significant control deficiencies identified during the year.

Issue	Commentary	Auditor view
<p><b>1 Castle House Valuation</b></p> <p>The Council occupies part of Castle House, new purpose built offices in Newcastle town centre. The land is owned by Newcastle-under-Lyme BC (NuLBC) and leased to Staffordshire County Council (SCC) under a headlease. SCC arranged for the construction of the building on this land. NuLBC then leased a portion of the building back from SCC via an underlease (the building is shared between SCC, NuLBC and the Police).</p> <p>Both leases are on the basis of a peppercorn rent. No amount is payable by NuLBC to SCC because the Council contributed towards the cost of constructing Castle House on the basis of the amount of the building which it would occupy, in return for which it would not be charged a rent. Payments to SCC towards the construction costs were mostly in 2016/17 (£2.159m) and 2017/18 (£2.035m); there may be a small amount payable in 2018/19 to cover outstanding payments to contractors but this is not expected to be material. In previous years the Council treated the expenditure in relation to the payments to SCC as REFCUS. Materiality for the 2018/19 audit is £1.25m.</p> <p>The Council moved into Castle House in 2018/19. On review of the arrangement during the year, the Council has determined that it should be classified as a finance lease and recognised on balance sheet. It has also determined that the amounts paid in prior year were upfront payments related to the lease and therefore the treatment as REFCUS in previous years was incorrect and a PPA was required.</p> <p>The building has been valued in 2018/19 by VOA, on the basis of it being held under a finance lease.</p>	<p>We are currently in discussions with the Council in obtaining the required evidence in order to allow us to determine the answers to a number of questions including:</p> <ul style="list-style-type: none"> <li>• Is the assessment that the portion of the building that NuLBC has the right to use is a finance lease appropriate?</li> <li>• Is the accounting treatment of the building as AUC prior to the lease commencement in 2018/19 appropriate, given its assessment as a finance lease but then accounted for as an owned asset i.e. AUC prior to the lease commencement date?</li> <li>• If treatment as AUC is not appropriate, would treatment as a prepayment be the most appropriate treatment prior to the lease commencement, with recognition in PPE (OL&amp;B) then taking place as an addition in 2018/19 following the commencement of the lease?</li> </ul> <p>The key to the accounting treatment is determining the Council's obligations – sufficient to support its rationale that the Council has 'control' over the asset at each of the balance sheet dates, such that it would be appropriate for it to account for it as an asset under construction.</p> <p>The Council has provided a copy of the specific terms of agreement and we will review this in arriving at our view.</p>	<p><b>Auditor view</b></p> <p>We remain in dialogue with the Council and will discuss the appropriate accounting in line with the accounting standards after review of the evidence provided.</p>



# Significant findings - other issues

This section provides commentary on new issues and risks which were identified during the course of the audit that were not previously communicated in the Audit Plan and a summary of any significant control deficiencies identified during the year.

Issue	Commentary	Auditor view
<p><b>2 Ryecroft Site (former Council Offices)</b></p> <p>Our review of the accounts identified that the valuations for:</p> <ul style="list-style-type: none"> <li>Former Civic Offices - £2,232,950 Operational Land and Buildings</li> <li>Former supermarket site - £330,255 Operational Land and Buildings</li> <li>Former Sainsbury's car park - £345,950 Investment Property</li> </ul> <p>had not changed from the prior year.</p> <p>The Council had not valued these assets as at the 31<sup>st</sup> March 2019 and continued to hold them as operational assets.</p>	<p>We have discussed our concerns with the Director of Finance and agreed that a revaluation of the former Civic Offices is required because:</p> <ul style="list-style-type: none"> <li>The offices were not operational and were in fact vacant and boarded up as at the 31<sup>st</sup> March 2019.</li> <li>The Council was aware of asbestos issues which would have a direct impact on the valuation of the building.</li> </ul> <p>The Council is in discussions with a private developer and this could impact the valuation.</p> <p>We have requested that the Council review the valuations and provide us with a paper setting out its proposed accounting treatment.</p>	<p><b>Auditor view</b></p> <p>We remain in dialogue with the Council and will discuss the appropriate accounting in line with the accounting standards after review of the evidence provided.</p>
<p><b>3 Jubilee 2 Leisure Centre</b></p> <p>In 2017/18 desktop valuations were carried out in respect of Jubilee 2 to establish whether it was considered there was material change in the previous years valuation figure of £8.9m.</p> <p>The valuation has been reviewed and revised in 2018/19. This valuation has been based on the build costs set out in Spons (Architects and Builders Price book) 2019, arriving at a valuation of £12m.</p>	<p>We have been in discussions with the Council's internal valuer and have found that:</p> <ul style="list-style-type: none"> <li>The Council has applied the incorrect Spons indices (incorrect data was published by Spons). This was identified as a consequence of our challenge of the significant increase in prices.</li> <li>The error extends to 38 other assets owned by the Council using the same valuation methodology.</li> </ul> <p>The Council are in the process of updating their valuations and providing response to our challenge questions on the valuations of individual assets. We have also requested additional evidence to demonstrate how valuations carried out at April 2018, have been updated, to reflect movement in values up to 31 March 2019.</p>	<p><b>Auditor view</b></p> <p>We remain in dialogue with the Council and will discuss the appropriate accounting in line with the accounting standards after review of the evidence provided.</p>

# Significant findings – key judgements and estimates

Accounting area	Summary of management's policy	Audit Comments	Assessment
<b>Provisions for NNDR appeals - £XXm</b>	Our work is currently underway and we will report on conclusion of our work.		●
<b>Land and Buildings – Council Housing - £XXm</b>	Our work is currently underway and we will report on conclusion of our work.		●
<b>Land and Buildings – Other - £XXm</b>	Our work is currently underway and we will report on conclusion of our work.		●
<b>Net pension liability – £XXm</b>	Our work is currently underway and we will report on conclusion of our work.		●

## Assessment

- We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- We consider management's process is appropriate and key assumptions are neither optimistic or cautious

# Significant findings – matters discussed with management

This section provides commentary on the significant matters we discussed with management during the course of the audit.

	Significant matter	Commentary	Auditor view
1	Significant events or transactions that occurred during the year	Our work is currently underway and we will report on conclusion of our work.	<b>Management response</b> • [...]
2	Business conditions affecting the Council, and business plans and strategies that may affect the risks of material misstatement	Our work is currently underway and we will report on conclusion of our work.	<b>Auditor view</b> • [...]
3	Concerns about management's consultations with other accountants on accounting or auditing matters	Our work is currently underway and we will report on conclusion of our work.	<b>Auditor view</b> • [...]
4	Discussions or correspondence with management in connection with the initial or recurring appointment of the auditor regarding accounting practices, the application of auditing standards, or fees for audit or other services	Our work is currently underway and we will report on conclusion of our work.	<b>Auditor view</b> • [...]
5	Significant matters on which there was disagreement with management, except for initial differences of opinion because of incomplete facts or preliminary information that are later resolved by the auditor obtaining additional relevant facts or information	Our work is currently underway and we will report on conclusion of our work.	<b>Auditor view</b> • [...]
6	Other matters that are significant to the oversight of the financial reporting process	Our work is currently underway and we will report on conclusion of our work.	<b>Auditor view</b> • [...]

# Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

	Issue	Commentary
1	<b>Matters in relation to fraud</b>	We have previously discussed the risk of fraud with the Audit and Standards Committee. We have not been made aware of any cases currently under investigation by the Council that could have a material impact on the financial statements. No other issues have been identified during the course of our audit procedures.
2	<b>Matters in relation to related parties</b>	We are not aware of any related parties or related party transactions which have not been disclosed.
3	<b>Matters in relation to laws and regulations</b>	You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
4	<b>Written representations</b>	A letter of representation will be requested from the Council. We will consider the need for specific representations after the completion of our fieldwork.
5	<b>Confirmation requests from third parties</b>	We requested from management permission to send requests to confirm year end bank and investment balances. This permission was granted and the requests were sent, and all received to confirm year end balances.
6	<b>Disclosures</b>	Our review found no material omissions in the financial statements, based on the work to date.
7	<b>Audit evidence and explanations/significant difficulties</b>	We encountered significant difficulties in the delivery of our audit due to a number of issues. Our audit remains in progress and we will update the Audit and Standards Committee after the conclusion of the audit. Working papers, particularly around PPE, required strengthening. The audit highlighted numerous issues which were fed back to staff and required re-working of working papers to make them fit for purpose.

# Other responsibilities under the Code

Issue	Commentary
① <b>Other information</b>	<p>We are required to give an opinion on whether the other information published together with the audited financial statements (including the Annual Governance Statement and Narrative Report, is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</p> <p>No inconsistencies have been identified, based on the work to date. We expect to issue an unmodified opinion in this respect – refer to appendix E.</p>
② <b>Matters on which we report by exception</b>	<p>We are required to report on a number of matters by exception in a numbers of areas:</p> <ul style="list-style-type: none"> <li>• If the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the other information of which we are aware from our audit; and</li> <li>• If we have applied any of our statutory powers or duties.</li> </ul> <p>We have nothing to report on these matters.</p>
③ <b>Specified procedures for Whole of Government Accounts</b>	<p>We are required to carry out specified procedures (on behalf of the NAO) on the Whole of Government Accounts (WGA) consolidation pack under WGA group audit instructions.</p> <p>This is not required at Newcastle under Lyme Borough Council as the Council does not exceed the threshold for 2018/19.</p>
④ <b>Certification of the closure of the audit</b>	<p>We intend to certify the closure of the 2018/19 audit of Newcastle under Lyme Borough Council in the audit opinion, as detailed in Appendix E, following the completion of our audit.</p>

# Value for Money

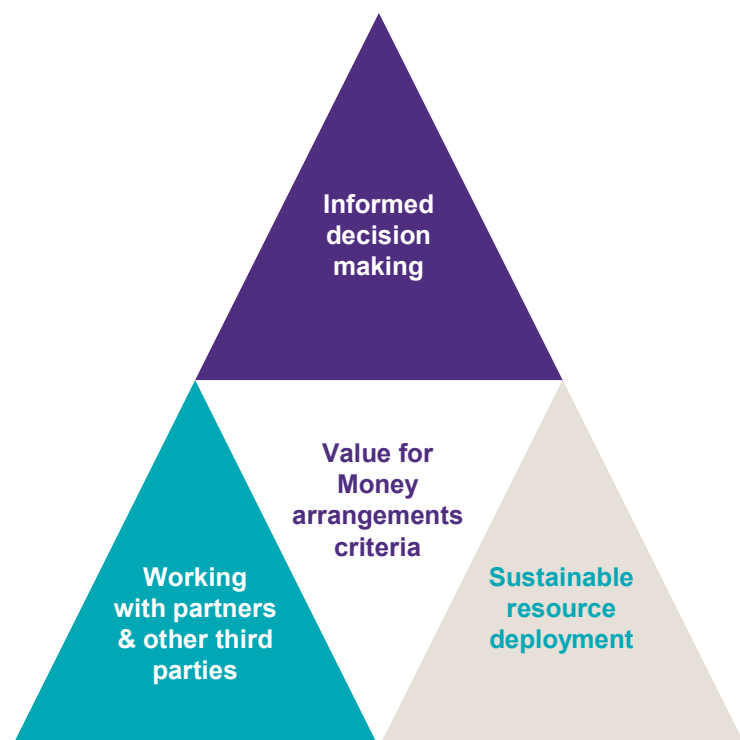
## Background to our VFM approach

We are required to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the Value for Money (VFM) conclusion.

We are required to carry out sufficient work to satisfy ourselves that proper arrangements are in place at the Council. In carrying out this work, we are required to follow the NAO's Auditor Guidance Note 3 (AGN 03) issued in November 2017. AGN 03 identifies one single 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."*

This is supported by three sub-criteria, as set out below:



## Risk assessment

We carried out an initial risk assessment in January 2019 and identified a number of significant risks in respect of specific areas of proper arrangements using the guidance contained in AGN03. We communicated these risks to you in our Audit Plan dated January 2019.

We have continued our review of relevant documents up to the date of giving our report, and have not identified any further significant risks where we need to perform further work.

# Value for Money

## Our work

AGN 03 requires us to disclose our views on significant qualitative aspects of the Council's arrangements for delivering economy, efficiency and effectiveness.

We have focused our work on the significant risks that we identified in the Council's arrangements. In arriving at our conclusion, our main considerations were:

- Review of the MTFS and the 2019/20 budget and assessment of the Authority's savings/income generation plans.
- Consideration of the independent investigations and the Council's response.

We have set out more detail on the risks we identified, the results of the work we performed, and the conclusions we drew from this work on pages 16 to 18.

## Overall conclusion

Based on the work we performed to date to address the significant risks, we are satisfied that the Council had proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

Our work remains ongoing at present.

## Recommendations for improvement

Our work remains in progress and we will discuss findings arising from our work with management and agree recommendations for improvement.

Our recommendations and management's response to these can be found in the Action Plan at Appendix A.

## Significant difficulties in undertaking our work

We did not identify any significant difficulties in undertaking our work on your arrangements which we wish to draw to your attention.

## Significant matters discussed with management

There were no matters where no other evidence was available or matters of such significance to our conclusion or that we required written representation from management or those charged with governance.



## Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

	Significant risk	Findings	Conclusion
1	<p><b>Financial sustainability</b></p> <p>The Medium Term Financial Strategy approved in October 2018 identified budgetary shortfalls of £1.9m in 2019/20 with further shortfalls in the years to 2023/24 totalling £3m. The 2019/20 budget has since been revised and now indicates an increased forecast shortfall of £2.2m, with £2.5m of potential savings identified in order to meet this.</p> <p>We will review the MTFS and the 2019/20 budget and assess the Authority's savings/income generation plans.</p> <p>We will review the outturn for 2018/19 and the Authority's track record of addressing budget shortfalls.</p>	<p><b><u>2018-19 Outturn:</u></b></p> <p>The unaudited outturn in respect of the General Fund Revenue Account was a surplus of £8,155 compared to the budget of £13,335,420. Whilst there were adverse variances against some budget heads, these have been offset by positive variances against others.</p> <p><b><u>2019-20 Position:</u></b></p> <p>The Council set a balanced budget for 2019-20 in line with requirements after developing plans to address the remaining budget deficit of £2.220 million.</p> <p>Management has confirmed that as at the end of June 2019 the Council is on track to achieve the savings approved as part of the 2019/20 budget setting process. However, the significant spend pressure from:</p> <ul style="list-style-type: none"> <li>• Overspends in waste and leisure from 2018-19.</li> <li>• Sickness management leading to increased use of agency staff and therefore incurring higher costs.</li> </ul> <p>This suggests the need to strengthen sickness management and monitoring procedures and to develop a corporate dashboard which includes a KPI in relation to sickness absence.</p> <p>In addition, the new Chief Exec has been consulting Heads of Service about changes to management structure. The proposal is to recruit to a number of senior posts including an Executive Director of Regeneration, Head of HR, Head of Planning, Head of Legal and Governance (Monitoring Officer). In addition the Council is also looking to recruit a full time Head of Finance (deputy S151) and a new role Head of Customer and Digital Service. There will be some cost savings required at levels below Head of Service to fund these.</p> <p>The Council's Section 151 Officer has recommended that a minimum level of un-earmarked reserves and contingencies of £1.548m be held to reflect the levels of revenue risk.</p> <p>Therefore, the Council's Balances and Reserves Strategy for 2019/20 is that there should be a minimum General Fund balance of £1.448m and a Contingency Reserve of £100,000.</p> <p>Management have identified that there are a number of spend pressures emerging for the year but mitigating action is being taken where possible and increased savings and/or income generation opportunities have also been identified.</p> <p><b><u>Forward Look:</u></b></p> <p>We are currently in the process of updating our assessment.</p>	<p>Our work remains in progress and we will consider our opinion on conclusion of the audit.</p>

## Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

	Significant risk	Findings	Conclusion
2	<p><b>Governance and capacity</b></p> <p>There has been an independent investigation into the arrangements at the last general election, and across-party investigation and disciplinary panel was setup to review the arrangements in place. Due to an unrelated matter the Executive Director (Resources and Support Services) is also currently suspended.</p> <p>The Authority needs to ensure such investigations are concluded in a timely manner, as well as ensuring that sufficient management capacity is maintained within the Authority to ensure effective and appropriate governance is maintained.</p> <p>We will monitor the investigations and the Council response to determine whether there are any implications for our VFM conclusion.</p>	<p><b>Arrangements at last general election</b></p> <p>The Council has received an independent report into the arrangements at the last general election and have been provided with a series of recommendations for implementation.</p> <p>Following the resignation of the Chief Executive in August 2018, the internal disciplinary investigation was suspended.</p> <p>A new Chief Executive has been subsequently been appointed, who commenced in post in February 2019.</p> <p>Our discussions with the Council have not identified any implications for our VFM conclusion.</p> <p><b>Executive Director - Resources</b></p> <p>The Council suspended the Executive Director (Resources &amp; Support Services) in October 2018 and an investigation remains underway. The Council has appointed external investigators to review the matters raised. It is important that this process is concluded in a timely manner.</p> <p>The Council have made an interim appointment whilst the investigations remains open in order to ensure that continuity of business is not affected.</p> <p>We will continue to maintain our regular dialogue with the Council and maintain a watching brief over the issues being considered.</p> <p>Our discussions with the Council have not identified any implications for our VFM conclusion.</p> <p><b>Statement of Accounts Preparation</b></p> <p>The difficulties experienced in carrying out the audit this year identified areas for improvement in the planning, oversight and delivery of the final accounts preparation process, which will need to be addressed going into 2019-20. These do not ,however, impact our overall VFM conclusion.</p>	<p><b>Auditor view</b></p> <p>Our work remains in progress and we will consider our opinion on conclusion of the audit.</p>

# Value for Money – Financial Resilience & Going concern

## Our responsibility

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK) 570).

## Going concern commentary

### Management's assessment process

Management have responded to the questions we set out on going concern in our “Informing the Audit Risk Assessment” document which confirms:

- There are no events, of which they are aware, that could cause sufficient material uncertainty to cast significant doubt on the Council's ability to continue as a going concern. This extends but is not limited to at least twelve months from the Balance Sheet date.
- The Council monitor cash flow on a daily basis, including maintaining an up to date forecast position for at least the next 12 months. The cash flow forecast provided to March 2020 does not indicate any material uncertainty relating to the Council's continuing ability to meet financial obligations.

### Work performed

Management's assessment was subject to arithmetical checks and reviewed for reasonableness of assumptions and predictions.

### Concluding comments

### Auditor commentary

CIPFA Code of Practice 2018/19 Code para 3.4.2.23 states "Local authorities that can only be discontinued under statutory prescription shall prepare their financial statements on a going concern basis of accounting; that is, the financial statements shall be prepared on the assumption that the functions of the authority will continue in operational existence for the foreseeable future".

The presumption in local government is that the going concern assumption does apply unless there is specific evidence to the contrary from factors such as an announcement to wind up the authority, failure to set a balanced budget, external assessment concludes unsustainable, financial plans show unable to meet obligations for foreseeable future or significant doubts over forward financial planning arrangements.

Management's assessment has considered these areas and concluded that no material uncertainty in respect of going concern exists. In addition based on our own knowledge of the Council we are aware that the Council has set an "approved budget" for 2019/20 and has a longer term financial plan. The cashflow forecast provided to March 2020 does not indicate any signs of significant financial difficulty that would cause concern.

We will require a cashflow forecast covering the 12 month period from the date of signing prior to our issuing of the opinion on the financial statements.

As such we consider that the assessment undertaken by the Council on going concern is a reasonable and valid one and there are no indications of material uncertainty.

### Auditor commentary

Our audit did not identify any events or conditions which may cast significant doubt on going concern assumption.

The Council set a budget in line with local government requirements for 2019-20 and whilst it's initial funding gap increased from £1.891 million to £2.220 million, it has identified potential savings of £2.468 million to mitigate this risk.

Management have confirmed as part of regular updates with them that at the end of June the Council is on track to achieve the savings approved as part of the 2019/20 budget setting process. However, management have identified that there are a number of spend pressures emerging for the year but mitigating action is being taken where possible and increased savings and/or income generation opportunities have also been identified.

### Auditor commentary

We expect to issue an unmodified opinion for 2018/19, following completion of our work.

# Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Financial Reporting Council's Ethical Standard and confirm that we, as a firm, and each covered person, are independent and are able to express an objective opinion on the financial statements

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in December 2017 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

Details of fees charged are detailed in Appendix D

### Audit and Non-audit services





For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The following non-audit services were identified, as well as the threats to our independence and safeguards that have been applied to mitigate these threats.

	Fees £	Threats identified	Safeguards
<b>Audit related</b>			
Certification of Housing benefit grant claim.	9,000	Self-Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work is £9,000 in comparison to the total fee for the audit of £42,352 and in particular relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors all mitigate the perceived self-interest threat to an acceptable level.




These services are consistent with the Council's policy on the allotment of non-audit work to your auditors. All services have been approved by the Audit & Standards Committee. None of the services provided are subject to contingent fees.

# Action plan

We have identified 8 recommendations to date for the Council as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2019/20 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.





Assessment	Issue and risk	Recommendations
1	 <p>Financial Statements Closedown</p> <p>The difficulties experienced in carrying out the audit this year identified areas for improvement in the planning, oversight and delivery of the final accounts preparation process, which will need to be addressed going into 2019-20.</p>	<p>The Council should review their accounts closedown process and ensure that improvements are made to ensure a smoother final statements audit in 2019-20.</p> <p><b>Management response:</b></p> <p>The accounts closedown process is reviewed every year to ensure that improvements are made wherever possible.</p>
2	 <p>Quality of Working Papers</p> <p>Working papers, particularly around PPE, required strengthening. The audit highlighted numerous issues which were fed back to staff and required re-working of working papers to make them fit for purpose.</p>	<p>The Council should review the quality of their working papers prior to making them available to audit.</p> <p><b>Management response:</b></p> <p>PPE working papers will be strengthened for next year. The procurement of an asset register system during 2019/20 will alleviate some of the issues that were encountered during 2018/19.</p>
3	 <p>Sickness Management Procedures</p> <p>High levels of sickness have lead to increased use of agency staff and therefore incurring higher costs for the Council.</p> <p>This suggests the need to strengthen sickness management and monitoring procedures and to develop a corporate dashboard which includes a KPI in relation to sickness absence</p>	<p>The Council should strengthen sickness management and monitoring procedures and develop a corporate dashboard which includes a KPI in relation to sickness absence.</p> <p><b>Management response</b></p> <p>A new Absence Management Policy has been approved.</p> <p>Payroll is in the process of being outsourced, a new system will enable managers to review absence via a dashboard system available on their desktop.</p>
4	 <p>Asset Register</p> <p>The Council does not have a formal capital asset register instead operating a spreadsheet based recording system.</p>	<p>The Council should consider investing in capital asset register software that meets the requirements of the Council going forward.</p> <p><b>Management response</b></p> <p>An Asset Management System will be procured during 2019/20 as a priority.</p>

## Controls

-  High – Significant effect on control system
-  Medium – Effect on control system
-  Low – Best practice

# Action plan

We have identified 8 recommendations to date for the Council as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2019/20 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

Assessment	Issue and risk	Recommendations
5	 <p><b>DEFRA Accrual</b></p> <p>The Authority has recognised grant income from DEFRA of £450k, and has incurred expenditure of £19,256 up to the end of the year. An accrual has been recognised in the accounts to reflect the fact that the balance of this grant expenditure will be paid in 19/20, relating to expenditure incurred in 2019/20. Accruals should not be recognised in anticipation of expenditure expected to be incurred in future years, and accruals/expenditure are therefore both overstated by £430,744.</p>	<p>Accruals should not be recognised in anticipation of expenditure expected to be incurred in future years.</p> <p><b>Management response:</b></p> <p>It is not proposed to change this treatment, it is below the materiality threshold. Alternative treatments will result in the same bottom line on the Income and Expenditure Statement and the same bottom line on the Balance Sheet.</p>
6	 <p><b>REFCUS – DFG Expenditure</b></p> <p>Audit testing identified that the current REFCUS DFG expenditure recognised as expenditure within the CIES of £1,574k can not be substantiated against evidence of DFG works undertaken by Millbrook Healthcare whom the Council have contracted with to deliver their DFG works. The Council has recognised a DFG spend amount to match the level of DFG grant allocation received in 2018-19. The Council is in discussion with Millbrook to try and obtain this information, but as at 4.7.2019 no year end statement has been received. The level of DFG expenditure recognised is material, and therefore there is currently an audit uncertainty over the accuracy of the amount recognised.</p>	<p>The Council should obtain the necessary evidence to support the expenditure recognised in the accounts.</p> <p><b>Management response:</b></p> <p>The Council is still in discussion with Millbrook, if monies that have been accrued are not payable to Millbrook they will be payable to Staffordshire County Council – there will be no impact on the accounts regardless of who the money is payable to.</p>
7	 <p><b>Asset Disposals</b></p> <p>Audit testing of PPE disposals identified that the Council incorrectly recognised a disposal for the IT servers of £697k. These were not disposed of when the Council moved to their new offices but were instead, transferred to a new location.</p>	<p>Asset disposals of £697k should be reversed as they have not been disposed off.</p> <p><b>Management response</b></p> <p>This has now been re-instated by the Property team.</p>
8	 <p><b>Recognition of Rental Income</b></p> <p>From our testing we identified that the Council had recognised rental income for one of their properties covering the period 25/03/19-25/06/19 in March '19, but no adjustments had been made to reverse the element relating to 2019/20. The invoice amount was £1,200 and therefore 12/13 of this sum should have been reversed out as income in advance. We have quantified this error by obtaining all similar invoices raised in advance, and this amounted to £192k.</p>	<p>Management should review rental income at year-end and ensure that it recognised in the correct period to which it relates.</p> <p><b>Management response</b></p> <p>It is not proposed to change this treatment, 12 months of income is included in the 2018-19 accounts as it has been for at least the previous 6 years.</p>

## Controls

- High – Significant effect on control system
- Medium – Effect on control system
- Low – Best practice

# Follow up of prior year recommendations

We identified the following issues in the audit of [insert client name] Council's 2017/18 financial statements, which resulted in [x] recommendations being reported in our 2017/18 Audit Findings report.

	Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
1	✓	The Council are currently undertaking a cross-party investigation and disciplinary panel in relation to the issues arising from the Council's delivery of the voting for the General Election in June 2017.	Management Comment: The former Chief Executive and Head of Elections have left the Council's employment. Recommendations have been implemented by the Elections team. Elections have since taken place without issue.
2	✓	Our work identified that 1 asset (value £8.936m) that has not been revalued within the last 5 years as required by the CIPFA Code of Practice.	Management Comment: A desktop valuation was completed in May 2018 to confirm that the valuation for 2017/18 was still applicable, a full revaluation was completed during 2018/19.

Assessment  
✓ Action completed  
X Not yet addressed



# Audit Adjustments - – TO BE INCLUDED FOLLOWING CONCLUSION OF AUDIT.

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

## Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year ending 31 March 2019.

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000
1	[...]	[...].	
2	[...]	[...].	
3	[...]	[...].	
Overall impact	£X,XXX	£X,XXX	£X,XXX

## Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Disclosure omission	Detail	Auditor recommendations	Adjusted?
	• [...]	• [...] Management response	✓

# Audit Adjustments - – TO BE INCLUDED FOLLOWING CONCLUSION OF AUDIT.

## Impact of unadjusted misstatements

The table below provides details of adjustments identified during the 2018/19 audit which have not been made within the final set of financial statements. The Committee is required to approve management's proposed treatment of all items recorded within the table below:

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000	Reason for not adjusting
1 [enter detail of adjustment]	[...]	[...].		
2 [enter detail of adjustment]	[...]	[...].		
Overall impact	£X,XXX	£X,XXX	£X,XXX	

## Impact of prior year unadjusted misstatements

The table below provides details of adjustments identified during the prior year audit which had not been made within the final set of 2017/18 financial statements.

Detail	Comprehensive Income and Expenditure Statement £'000	Statement of Financial Position £' 000	Impact on total net expenditure £'000	Reason for not adjusting
1 [enter detail of adjustment]	[...]	[...].		
2 [enter detail of adjustment]	[...]	[...].		
Overall impact	£X,XXX	£X,XXX	£X,XXX	

# Fees

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

<b>Audit Fees</b>	<b>Proposed fee</b>	<b>Final fee</b>
<b>Council Audit – as reported in our fee letter</b>	£42,352	£42,352
<b>Total audit fees (excluding VAT)</b>	<b>£42,352</b>	<b>£42,352</b>
<b>Fee Variations – National Issues:</b>		
Assessing the impact of the McCloud ruling - The Government's transitional arrangements for pensions were ruled discriminatory by the Court of Appeal last December. The Supreme Court refused the Government's application for permission to appeal this ruling. As part of our audit we considered the impact on the financial statements along with any audit reporting requirements.	<b>£1,500</b>	<b>TBC</b>
Pensions – IAS 19 - The Financial Reporting Council has highlighted that the quality of work by audit firms in respect of IAS 19 needs to improve across local government audits. Accordingly, we have increased the level of scope and coverage in respect of IAS 19 this year.	<b>£1,500</b>	<b>TBC</b>
PPE Valuation – work of experts - The Financial Reporting Council has highlighted that auditors need to improve the quality of work on PPE Valuations across the sector. We have increased the volume and scope of our audit work to reflect this.	<b>£1,500</b>	<b>TBC</b>
<b>Revised total audit fee (excluding VAT)</b>	<b>£45,586</b>	<b>TBC</b>
<b>Fee Variations – Local Issues</b>		
The Newcastle under Lyme Borough Council has required significant additional audit resources as a result of the valuation issues and poor working papers provided for the 2018-19 audit. We will confirm the additional fee requirements following the conclusion of the audit.	<b>TBC</b>	<b>TBC</b>
<b>Revised total audit fee (excluding VAT)</b>	<b>TBC</b>	<b>TBC</b>

All of the national fee variations above have been driven by additional work required as the result of either sector challenges or in response to FRC feedback not as the result of weaknesses in the Council's arrangements in the preparation of its financial statements. In contrast, the local fee variations relate directly to issues at Newcastle under Lyme Borough Council. The revised fee for the year is subject to approval by Public Sector Appointments Ltd (PSAA).

## Non Audit Fees

<b>Grant Certification</b>	<b>Fees £</b>
Certification of Housing benefit grant claim.	9,000

Our fees for grant certification cover only housing benefit subsidy certification, which falls under the remit of Public Sector Audit Appointments Limited.

## Audit opinion – TO BE INCLUDED FOLLOWING CONCLUSION OF AUDIT.

We anticipate we will provide the Council with an unmodified audit report [or amend as appropriate]

INSERT FULL TEXT OF THE DRAFT OPINION

# Audit opinion - – TO BE INCLUDED FOLLOWING CONCLUSION OF AUDIT.

INSERT FULL TEXT OF THE DRAFT OPINION FROM TEMPLATE ON ONEPLACE

## **Management Letter of Representation – TO BE INCLUDED FOLLOWING CONCLUSION OF AUDIT.**

