



The Annual Audit Letter for Newcastle-under-Lyme Borough Council

Year ended 31 March 2020

January 2021



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Executive Summary

Purpose

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at Newcastle-under-Lyme Borough Council (the Council) for the year ended 31 March 2020.

This Letter is intended to provide a commentary on the results of our work to the Council and 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 and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'. We reported the detailed findings from our audit work to the Council's Audit and Standards Committee as those charged with governance in our Audit Findings Report on 9 November.

Our work

Materiality	We determined materiality for the audit of the Council's financial statements to be £1,185,000, which is 2% of the Council's gross cost of services.
Financial Statements opinion	We gave an unqualified opinion on the Council's financial statements on 27 November 2020. We included an emphasis of matter paragraph in our report in respect of the uncertainty over valuations of the Council's land and buildings and the property assets of its pension fund given the Coronavirus pandemic. This does not affect our opinion that the statements give a true and fair view of the Council's financial position and its income and expenditure for the year.
Whole of Government Accounts (WGA)	We completed work on the Council's consolidation return following guidance issued by the NAO.
Use of statutory powers	We did not identify any matters which required us to exercise our additional statutory powers.
Value for Money arrangements	We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources. We reflected this in our audit report to the Council on 27 November 2020.
Certificate	We certified that we have completed the audit of the financial statements of Newcastle-under-Lyme Borough Council in accordance with the requirements of the Code of Audit Practice on 27 November 2020.

Respective responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, 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 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 financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

Executive Summary

Working with the Council

The Covid-19 pandemic has impacted on the Council operational with the majority of its staff working remotely. Restrictions for non-essential travel and social distancing has meant both Council and audit staff have had to complete the audit through remote access working arrangements i.e. remote accessing financial systems, video calling and additional procedures in relation to the completeness and accuracy of information produced by the entity. Both the Council and audit team have responded well to the challenges posed to ensure completion of the audit work.

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

Audit of the Financial Statements

Our audit approach

Materiality

In our audit of the Council's financial statements, 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 the audit of the Council's financial statements to be £1,185,000, which is 2% of the Council's gross cost of services. We used this benchmark as, in our view, users of the Council's financial statements are most interested in where the Council has spent its revenue in the year.

We also set a lower level of specific materiality for senior officer remuneration of £18,000.

We set a lower threshold of £59,000, above which we reported errors to the Audit and Standards Committee in our Audit Findings Report.

The scope of our audit

Our audit involves obtaining sufficient 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 accounting policies are appropriate, have been consistently applied and adequately disclosed;
- the 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 remainder of the Statement of Accounts to check it is consistent with our understanding of the Council and with the financial statements included in the Statement of Accounts on which we gave our opinion.

We carry out our audit in accordance with ISAs (UK) and the NAO Code of Audit Practice. We believe that 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 Financial Statements

Significant Audit Risks

These are the significant 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	Findings and conclusions
<p>Covid-19</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> worked with management to understand the implications the response to the Covid-19 pandemic had on the organisation's ability to prepare the financial statements and update financial forecasts and assessed the implications for our materiality calculations. No changes were made to materiality levels previously reported. The draft financial statements were provided on time in July 2020; liaised with other audit suppliers, regulators and government departments to co-ordinate practical cross-sector responses to issues as and when they arose. Examples include the material uncertainty disclosed by the Council/groups' property valuation expert evaluated the adequacy of the disclosures in the financial statements that arose in light of the Covid-19 pandemic; evaluated whether sufficient audit evidence could be obtained through remote technology; evaluated whether sufficient audit evidence could be obtained to corroborate significant management estimates such as assets and the pension fund liability valuations ; evaluated management's assumptions that underpin the revised financial forecasts and the impact on management's going concern assessment; 	<p>Our audit work has not identified any issues in respect of Covid-19</p>
<p>Management override of internal controls</p>	<p>As part of our audit work we completed;</p> <ul style="list-style-type: none"> evaluated the design effectiveness of management controls over journals analysed the journals listing and determine the criteria for selecting high risk unusual journals tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration gained an understanding of the accounting estimates, critical judgements applied and decisions made by management and consider their reasonableness with regard to corroborative evidence evaluated the rationale for any changes in accounting policies or significant unusual transactions. 	<p>Our audit work has not identified any issues in respect of management override of controls.</p>

Audit of the Financial Statements

Significant Audit Risks - continued

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	Findings and conclusions
<p>Valuation of land and buildings</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> evaluated the processes, controls and assumptions put in place by management to ensure that the PPE valuation is not materially misstated and evaluate the design of these and whether they are sufficient to mitigate the risk of material misstatement; assessed the competence, capabilities and objectivity of management's experts (valuers) who carried out your PPE valuations; evaluated the instructions issued by management to their management expert (a valuer) for this estimate and the scope of the valuer's work; communicated with the valuer about the basis on which the valuation is carried out and where necessary challenge the key assumptions reviewed and challenged the information used by the valuer to ensure it is robust and consistent with our understanding tested revaluations made during the year to ensure they are consistent with the valuer's report and 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 have satisfied themselves that these are not materially different to current value 	<p>The Council's valuer prepared their valuations as at 31 March 2020. In their reports, they have confirmed that as a result of the Covid-19 pandemic and the subsequent lockdown and impact on market activity, less certainty – and a higher degree of caution – should be attached to their valuations than would normally be the case. Their valuations are reported on the basis of 'material valuation uncertainty'.</p> <p>We referred to these material valuation uncertainties in our audit report as an emphasis of matter.</p> <p>Our testing also identified a number of amendments in relation to property, plant and equipment resulting in an increase of £572k for land & buildings and an decrease of £825k for investment properties.</p>

Audit of the Financial Statements

Significant Audit Risks - continued

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	Findings and conclusions
<p>Valuation of net pension liability</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • updated our understanding of the processes and controls put in place by management to ensure that the Authority's pension fund net liability is not materially misstated and evaluate the design of the associated controls; • evaluated the instructions issued to the management expert (actuary) for this estimate and the scope of the actuary's work; • assessed the competence, capabilities and objectivity of the actuary who carried out the Authority's pension fund valuation; • assessed the accuracy and completeness of the information provided by the Authority to the actuary, through the Pension Fund, to estimate the liability; • 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; • undertaken procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report; and • documented and evaluated 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. 	<p>The Council included disclosures in its Financial Statement in relation to the ongoing impact of the Covid-19 pandemic, which has created uncertainty surrounding illiquid asset values. As such, the Pension Fund property and infrastructure allocations as at 31 March 2020 are difficult to value. Professional valuers have not been actively valuing many similar sized assets in the market due to the current lockdown environment. As such values have been rolled over from the end of February with an adjustment and may be inaccurate to the true 31 March 2020 position.</p> <p>We referred to these material valuation uncertainties in our audit report as an emphasis of matter.</p> <p>Our other audit work has not identified any other issues in respect of the valuation of the Council's pension fund net liability</p>

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the Council's financial statements on 27 November 2020.

Preparation of the financial statements

The Council presented us with draft financial statements in August in accordance with the agreed timescale, and provided a good set of working papers to support them. The finance team responded promptly and efficiently to our queries during the course of the audit.

Issues arising from the audit of the financial statements

We reported the key issues from our audit to the Council's Audit and Standards Committee on 9 November 2020.

In addition to the key audit risks reported above, we identified a number of issues throughout our audit that we have asked the Council's management to address for the next financial year. Details of these issues and our recommendations including responses from management can be found in Appendix B.

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 in the Statement of Accounts in line with the national deadlines

Both documents were prepared in line with the CIPFA Code and relevant supporting guidance. We confirmed that both documents were consistent with the financial statements prepared by the Council and with our knowledge of the Council.

Whole of Government Accounts (WGA)

We carried out work in line with instructions provided by the NAO . We issued an assurance statement which confirmed the Council was below the audit threshold

Other statutory powers

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 did not identify any matters which required us to exercise our additional statutory powers.

Certificate of closure of the audit

We certified that we have completed the audit of the financial statements of Newcastle-under-Lyme Borough Council in accordance with the requirements of the Code of Audit Practice on 27 November 2020.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice, following the guidance issued by the NAO in April 2020 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 risks where we concentrated our work.

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

Overall Value for Money 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 2020. .

Value for Money conclusion

Significant risk

Financial Sustainability (Based on the Audit Plan)

The Council's latest medium term financial plan has significantly reduced the funding gap over the medium term to £0.49m in 2021/22; £0.327m in 2022/23; £0.308m in 2023/24; and £0.048m in 2024/25.

The CIPFA Financial Resilience Index, which looks at a range of factors that may affect resilience and sustainability, and relies on information on earmarked reserves, shows that the Council are at a higher risk compared to its nearest neighbours based on level and use of reserves. The Index also shows that the Council's business rates growth above the baseline is below the average of its nearest neighbours, which means the Council is less exposed to the business rates reset expected in 2021.

The medium term financial planning process is challenging due to the uncertainty over future local government funding arrangements as well as uncertain economic conditions. The longer-term reforms for the local government finance system, including business rates retention and fairer funding have been delayed until 2021/22 and the Council recognises the significant risk that these reforms, including the planned Business Rates Reset, will have a significant effect on the Council's funding level from 2021/22.

Findings

2019-20 Outturn:

The unaudited outturn in respect of the General Fund Revenue Account was an adverse variance of £0.207m compared to the budget of £13.050m. Whilst there were adverse variances against some budget heads, these have mainly been offset by positive variances against others. The main reason for the overspend at the end of the was due to Covid-19 pressures that resulted in reduced income from Jubilee 2, car parks and a hold on recovery actions in March 2020.

2020-21 Position and MTFS to 2025/26:

The Council have set a balanced budget for 2020-21. The ongoing pandemic has put additional pressures on this budget. Cabinet receive regular reports on Council's response to the pandemic and the delivery of its recovery plan.

The latest recovery plan update (October 2020) is forecasting a net overspend of £333k for the year, which will be funded from reserves. The main impact is due to lost income (e.g. car parking and Jubilee2 Leisure Centre), which over the first 2 quarters of the year is estimated at £2.292m. The Government is funding lost income at 75p per £1 lost above the first 5%. The Council have calculated that they will receive £1.558m leaving a shortfall of £0.734m which is included in the net overspend above.

Looking forward to 2021/22 and beyond the Council have recently updated its MTFS. This shows a gap of £5.911m over the next five years. For 2021/22 the gap is £1.790m, which is an increase from £1.367m from the previous MTFS due to pressures from Covid-19 pandemic.

The Council are working to address the 2020/21 as part of the budget setting process and to date they have identified £1.469m of savings. Draft savings proposals will be presented to Cabinet in December 2020.

Value for Money conclusion

Findings (continued)

To ensure that the Council is able to operate effectively and meet its strategic aims within its current environment they have commissioned consultants to undertake a review of how the Council will operate going forward. This review has recently been completed and the future operating model developed has identified circa £900k of savings. Officers are currently working through the recommendations and will incorporate them into the budget setting process.

As part of the MTFs the S151 officer has undertaken a risk based review of the minimum level of reserves required. This review identified that for 2021/22 the minimum level of reserves required is £3.116m. The Council currently have £1.584m. This risk assessment were completed prior to the second lockdown.

Conclusion

Auditor view

Like most of local government, the authority faces a challenging future driven by funding reductions and an increase in demand for services. This is further complicated by the ongoing pandemic which is placing additional pressures on the Council both financially and the challenges in providing services.

As we highlighted in 2018/19 the authority will need to continue to make tough decisions to deliver balanced budgets over the coming years, but also maintain strict budgetary control to minimise overspends and continue to monitor delivery of savings targets tightly.

The Council also need to continue to build reserves to become more financially resilience.

A. Reports issued and fees

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

Reports issued

Report	Date issued
Audit Plan	February 2020
Audit Findings Report	November 2020
Annual Audit Letter	January 2021

Fees

	Planned £	Actual fees £	2016/17 fees £
Statutory audit	£49,852	£59,822	£55,002
Total fees	£49,852	£59,822	£55,002

Audit fee variation

As outlined in our audit plan, the 2019-20 scale fee published by PSAA of £42,352 assumes that the scope of the audit does not significantly change. There are a number of areas where the scope of the audit has changed, which has led to additional work. These are set out in the following table. Fee variations are subject to PSAA approval.

Area	Reason	Fee proposed
Raising the Bar	The Financial Reporting Council (FRC) has highlighted that the quality of work by all audit firms needs to improve across local audit. This will require additional supervision and leadership, as well as additional challenge and scepticism in areas such as journals, estimates, financial resilience and information provided by the entity.	£2,500
Pensions – valuation of net liabilities under International Auditing Standard (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 to reflect this. Specifically, we have increased the granularity, depth and scope of coverage, with increased levels of sampling, additional levels of challenge and explanations sought, and heightened levels of documentation and reporting.	£1,750
PPE Valuation – Work of Experts	We have increased the volume and scope of our audit work to ensure an adequate level of audit scrutiny and challenge over the assumptions that underpin PPE valuations.	£1,750

A. Reports issued and fees continued

Area	Reason	Fee proposed
New Standards	We undertook work in preparation of the introduction of IFRS16. IFRS16 requires a leased asset, previously accounted for as an operating lease off balance sheet, to be recognised as a 'right of use' asset with a corresponding liability on the balance sheet. The introduction of IFRS16 was originally planned for 1 April 2020, however this has subsequently be delayed to 1 April 2021.	£1,500
Covid-19	Covid-19 has impacted on the audit of your financial statements in several ways. These impacts include: <ul style="list-style-type: none"> • Revisiting our audit planning • Additional work on management's assumptions and estimates • Additional work on our financial resilience assessment • Remote working 	£9,970
Total		£17,470

Fees for non-audit services

Service	Planned fee £
Audit related services	£11,400
- Housing Benefit (Subsidy) Assurance Process	
Non-Audit related services	
- None	

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 table above summarises all non-audit services which were identified.
- We have considered whether non-audit services might be perceived as a threat to our independence as the Council's auditor and have ensured that appropriate safeguards are put in place.

The above non-audit services are consistent with the Council's policy on the allotment of non-audit work to your auditor

B. Recommendations and Action Plan

We have identified two recommendations 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 2020/21 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
● Medium	Investment Properties The Council have applied a rolling programme of revaluation for Investment Property. Investment Property assets with a carrying value of £6.5m have not been subject to a formal valuation at 31st March 2020. Per the CIPFA Code of Practice and IFRS13 Investment Property should be measured at fair value at the reporting date, therefore a rolling programme of revaluation is not appropriate.	The Council should ensure that all assets categorised as investment properties are revalued on an annual basis to comply with the CIPFA Code of Practice and IFRS13. Management response All of the Investment Property assets have been reviewed during the year by the Council's Valuer. The Council has noted the recommendation that all of the assets reviewed should be formerly documented even if there is no change to the value as per the CIPFA Code of Practice.
● Medium	Vehicles, Plant, Furniture and Equipment (VPFE) From our testing we identified that 75% of VPFE have been fully depreciated but are still in use by the Council. Thus we deem the useful lives currently being allocated to VPFE (5-15 years) as too short and not reflective of their actual lives.	That the Council review the useful lives of its VPFE assets to ensure that they more accurately reflect the actual lives. Management response As the Council wants to ensure maximum use of its vehicle, plant, furniture and equipment, it has now reviewed the life of these assets to reflect their actual lives.

Controls

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



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