

The Annual Audit Letter for Nottinghamshire County Council and Nottinghamshire County Council Pension Fund

Year ended 31 March 2019

11 September 2019



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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 Nottinghamshire County Council and Nottinghamshire Pension Fund for the year ended 31 March 2019.

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 Governance and Ethics Committee as those charged with governance in our Audit Findings Report on 24 July 2019

Our work

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 and Pension Funds 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 and Pension Fund's financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

Materiality - Council	We determined materiality for the audit of the Councils financial statements to be £20m, which is 1.9% of the Council's gross revenue expenditure.
Materiality – Pension Fund	We determined financial statement materiality based on a proportion of the Pension Fund's net assets. Our materiality for the audit was £54m which equates to 1% of your actual net assets for the year ended 31 March 2019
Financial Statements opinion	We gave an unqualified opinion on the Council's and Pension Fund's financial statements on 31 July 2019.
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.

Executive Summary

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 31 July 2019.
Certificate	<p>We are unable to certify that we have completed the audit of the financial statements of Nottinghamshire County Council and Nottinghamshire Pension Fund until:</p> <ul style="list-style-type: none">the Council has prepared the Pension Fund Annual Report and we have issued the required report to say that it is consistent with the audited pension fund financial statementsyour previous auditors, KPMG, have completed their consideration of an objection to the 2015/16 accounts made by a local elector.

Working with the Council

This has been our first year as your external auditors. We aimed to achieve a smooth transition from your previous auditors, KPMG, and have worked closely with your officers throughout the year to ensure we were able to deliver our opinions and VFM conclusion to enable you to publish your Statement of Accounts by the 31 July deadline.

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
September 2019

Audit of the Financial Statements

Our audit approach

Materiality

In our audit of the Council and Pension Funds 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 Pension Funds financial statements to be £54m, which is 1% of the funds net assets. We determined materiality for the audit of the Council's financial statements to be £20m, which is 1.9% of the Council's gross revenue expenditure. .

We also set a lower level of specific materiality for the council in relation to senior officer remuneration - using a materiality of £100,000.

We set a lower threshold of £3m for the Pension Fund and £1m for the Council, above which we reported errors to the Governance and Ethics 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 financial statements and the Narrative Report and the Annual Governance Statement published alongside the financial statements to check they are consistent with our understanding of the Council and with the financial statements 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 and Pension Fund'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 - Council

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>Valuation of land and buildings</p> <p>The Authority revalues its land and buildings on a five-yearly basis. In the intervening years, such as 2018/19, 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, the Authority carries out a desktop revaluation or requests a desktop valuation from its valuation expert to ensure that there is no material difference. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£717 million) and the sensitivity of this estimate to changes in key assumptions.</p> <p>We therefore identified valuation of land and buildings as a significant risk.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none">• evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work• evaluated the competence, capabilities and objectivity of the valuation expert• written to the valuer to confirm the basis on which the valuation was carried out to ensure that the requirements of the Code have been met• challenged the information and assumptions used by the valuer to assess completeness and consistency with our understanding	<p>Our audit work has not identified any issues in respect of valuation of land and buildings</p>

Audit of the Financial Statements

Significant Audit Risks - Council

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>Valuation of net pension liability</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 (£1.1bn in the Authority's balance sheet) and the sensitivity of the estimate to changes in key assumptions.</p> <p>We therefore identified valuation of the Authority's pension fund net liability as a significant risk, which was one of the most significant assessed risks</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 evaluated the design of the associated controls;• evaluated the instructions issued by management to their management expert (an 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 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;• 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• agreed the advance payment made to the pension fund for future years to the expected accounting treatment and relevant financial disclosures.• considered the specific methodology and assumptions used by the actuary in relation to the McCloud case.	<p>During the course of our audit, there were significant developments in relation to a legal case, the McCloud case, on alleged age discrimination in transitional arrangements in public sector pension schemes. The Government was refused leave to appeal the Court's decision, increasing the likelihood of increase future pension payments.</p> <p>As a result, you obtained an updated actuarial report which estimated the impact of the McCloud case and resulted in an amendment to the accounts of an increase in pension liabilities of £44.8m and an increase in past service costs for the 2018/19 year of £21.1m.</p> <p>Pension Fund</p> <p>The Pension Fund has amended its disclosure in relation to the impact of the McCloud ruling resulting in a £65,9m increase in the disclosure of the net liability</p>

Audit of the Financial Statements

Significant Audit Risks – Council and Pension Fund

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>Management override of internal controls</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. The Authority and Fund faces external scrutiny of its spending and this could potentially place management under undue pressure in terms of how they report performance.</p> <p>We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk for both the Authority and Fund, which was one of the most significant assessed risks of material misstatement.</p>	<p>As part of our audit work we;</p> <ul style="list-style-type: none">• evaluated the design effectiveness of management controls over journals• analysed the journals listing and determined the criteria for selecting high risk unusual journals• gained an understanding of the accounting estimates and critical judgements applied made by management and considered their reasonableness with regard to corroborative evidence• evaluated the rationale for any changes in accounting policies, estimates 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

Pension Fund Significant Audit Risks

This are the risks which had the greatest impact on our overall strategy and where we focused more of our work on the pension fund

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Valuation of Level 3 (hard to value) Investment Assets</p> <p>Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none">• gained an understanding of the Fund's process for valuing level 3 investments and evaluated the design of the associated controls;• reviewed the nature and basis of estimated values and considered what assurance management have had over the year end valuations provided for these types of investments• for a sample of investments, tested the valuation by obtaining and reviewing the audited accounts (where available) at the latest date for individual investments and agreeing those to the fund managers reports at that date• there were a number of funds which are not overseen by the custodian, we have reviewed fund manager returns to gain assurance in these areas	<p>Our audit work has not identified any significant issues in relation to hard to value investments.</p> <p>We did, however, make some recommendations to improve some of the disclosures around investments and other areas within the Pension Fund accounts, and also in relation how the Fund obtains assurances from fund managers in relation to the controls which they have in place.</p>

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the Council's financial statements on 31 July 2019.

Preparation of the financial statements

The Council presented us with draft financial statements in accordance with the national deadline, 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 Governance and Ethics Committee on 24 July 2019.

Other than as noted above in relation to the impact of the McCloud case on the estimated pension fund liability, we did not identify any significant changes required to either the Council or Pension Fund financial statements, but we did request some further improvements to some of the disclosure notes within both sets of accounts.

Annual Governance Statement and Narrative Report

We are required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website in and alongside 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 on the Council's Data Collection Tool in line with instructions provided by the NAO . We issued an assurance statement which did not identify any issues for the group auditor to consider on 16 August 2019.

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.

Certificate of closure of the audit

We are unable to certify that we have completed the audit of the financial statements of Nottinghamshire County Council and Nottinghamshire Pension Fund until:

- the Council has prepared the Pension Fund Annual Report and we have issued the required report to say that it is consistent with the audited pension fund financial statements
- your previous auditors, KPMG, have completed their consideration of an objection to the 2015/16 accounts made by a local elector.

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 November 2017 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 2019.

Value for Money conclusion

Risks identified in our audit plan	Findings	Conclusions
<p>Financial Sustainability</p> <p>The council continues to face similar financial pressures to those experienced by others in the Local Government sector. The council's latest financial monitoring report (M08) presented to the Finance and Major Contracts Management Committee indicates a £5.8m net overspend forecast for the current financial year.(2018/19) Furthermore the council faces significant financial challenges over the medium term to achieve its statutory break even budget duty.</p> <p>The latest report shows a £34.1m gap for the medium term.</p>	<p>The Council has been successful in delivering £26.8m of savings over the previous two financial years. Rising demand for services coupled with continued reductions in funding will mean that savings will become increasingly more difficult to find.</p> <p>The financial position of the Council has been closely monitored throughout the year, with monthly reports being produced and reported to the Leadership Team and the Finance and Major Contracts Committee.</p> <p>The impact of pressures on social care services has resulted in a year end contribution from reserves of £6.8m compared to the £1.5m budgeted estimate.</p> <p>The MTFS proposes to utilise a further £19.2m of reserves over the medium term.</p> <p>The level of reserves and balances have been reviewed by the Council and are considered to be adequate. However the continued use of reserves to balance budgets which continues into 2019/20 should be approached cautiously and the Council should ensure that the level of reserves remain prudent. Reserves are one off funds so it is recommended that they are limited to supporting one-off expenditure rather than funding on-going costs</p> <p>The budget set for 2019/20 shows a savings requirement of £15.2m. The Council continues to monitor and gain understanding of both overspends and underspends against budgets and continually applies mitigation strategies, not only for the immediate budget but for the Medium Term to ensure the £34.2 shortfall forecast required by 2023 is addressed.</p> <p>Strict budgetary control is in place and departments are expected to utilise any underspends to offset unexpected cost pressures.</p>	<p>The Council applies a stringent monitoring regime to ensure issues can be identified and addressed in a timely manner. The MTFS is monitored and aligned to the vision of the Council and adjustments made when necessary.</p> <p>On the basis of this evidence we have concluded that the Council had appropriate arrangements in place to secure Value for Money through Sustainable Resource Deployment during 2018/19.</p>

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	Findings	Conclusions
<p>Partnership Working</p> <p>Increasingly the Council has identified and indeed continues to identify a range of measures and significant savings to mitigate financial challenges. It has increased partnership working with other public sector organisations in Nottinghamshire, across both local government and the NHS. The council has also made greater use of subsidiaries, joint ventures and its dedicated performance and improvement team.</p> <p>As wider partnership working evolves it is important to consider governance arrangements within the collaborations and ensure the required outcomes are being achieved.</p>	<p>The Council is committed to working with partners to provide the best possible services for local people whilst delivering value for money.</p> <p>Partnership working is diverse and covers health, the environment including transport and education.</p> <p>The health partnership as part of the Integrated Care System has notably seen an increase in the amount of service users enabled to return to independent living via the enablement service. Users of this service rose to 1,335 in 2018/19.</p> <p>The Council appoint representatives to a wide range of bodies to ensure that partnership working is monitored and governance is in place.</p> <p>The Policy Committee receive regular updates on the strategies and monitoring of partnerships and also a register of outside bodies with representatives is produced for their scrutiny. These bodies include local community groups charities and partners, and detail who is the council representative on each group.</p> <p>For example, a major partnership is the Integrated Care System. The board of the ICS includes a Nottinghamshire County Council representative, but also individual members such as Sherwood Forest Hospital FT also has a Council representative on its board.</p> <p>The council have had some major achievements during 2018/19 in relation to working with partners. These include leadership of the Partnership Strategy for looked after children and care leavers – becoming the first 2 tier council area to secure council tax exemption for its care leavers up to 25 – and the successful leadership and establishment of the Regional Adoption Agency.</p>	<p>Partnership working continues to achieve positive results for the Nottinghamshire area.</p> <p>This has improved services and in relation to health where the most pressure is felt financially and has provided closer integration. As a result the Council has been noted as the best performing council nationally for performance of delayed transfer of care.</p> <p>Governance is reported regularly to the Policy Committee and monitored by individual representatives.</p> <p>On the basis of this evidence we have concluded that the Council had appropriate arrangements in place to secure Value for Money through Partnership Working during 2018/19</p>

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	March 2019
Audit Findings Report	July 2019
Annual Audit Letter	August 2019

Fees

	Planned £	Actual fees £
Statutory audit	75,624	83,124
Audit of Pension Fund	23,043	23,043
Total fees	98,667	106,167

Audit fee variation

As outlined in our audit plan, the 2018-19 scale fee published by PSAA of £98,667 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.

Area	Reason	Fee proposed
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 have reviewed the revised actuarial assessment of the impact on the financial statements along with any audit reporting requirements.	3000
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 to reflect this.	1500
PPE Valuation – work of experts	As above, 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.	3000
Total		7500

Fee variations are subject to PSAA approval.

A. Reports issued and fees continued

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

Fees for non-audit services

Service	Fees £
Non-audit services CFO insights	10,000
Audit-related services IAS19 assurances to other auditors	6,000
	16,000

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 Councils auditor and have ensured that appropriate safeguards are put in place.

Grant Thornton's Government and Infrastructure Advisory Team has undertaken work for the Midlands Engine (a partnership of local authorities and other bodies (across the East and West Midlands) in relation to Support for the Business Case for a Development Corporation in relation to the HS2 hub at Toton. This specific piece of work was procured through Nottinghamshire County Council, but in doing so it was acting as agent for the entities that make up the 'Midlands Engine'. We are satisfied that this work does not present any threat to our independence as auditors of the County Council. The fee for this work, which was all paid in 2019/20, was £465,669.

Our commitment to our local government clients

- Senior level investment
- Local presence enhancing our responsiveness, agility and flexibility.
- High quality audit delivery
- Collaborative working across the public sector
- Wider connections across the public sector economy, including with health and other local government bodies
- Investment in Health and Wellbeing, Social Value and the Vibrant Economy
- Sharing of best practice and our thought leadership.
- Invitations to training events locally and regionally – bespoke training for emerging issues
- Further investment in data analytics and informatics to keep our knowledge of the areas up to date and to assist in designing a fully tailored audit approach

Our relationship with our clients– why are we best placed?

- We work closely with our clients to ensure that we understand their financial challenges, performance and future strategy.
- We deliver robust, pragmatic and timely financial statements and Value for Money audits
- We have an open, two way dialogue with clients that support improvements in arrangements and the audit process
- Feedback meetings tell us that our clients are pleased with the service we deliver. We are not complacent and will continue to improve further
- Our locally based, experienced teams have a commitment to both our clients and the wider public sector
- We are a Firm that specialises in Local Government, Health and Social Care, and Cross Sector working, with over 25 Key Audit Partners, the most public sector specialist Engagement Leads of any firm
- We have strong relationships with CIPFA, SOLCAE, the Society of Treasurers, the Association of Directors of Adult Social Care and others.

New opportunities and challenges for your community

The Local Government economy

Local authorities face unprecedented challenges including:

- Financial Sustainability – addressing funding gaps and balancing needs against resources
- Service Sustainability – Adult Social Care funding gaps and pressure on Education, Housing, Transport
- Transformation – new models of delivery, greater emphasis on partnerships, more focus on economic development
- Technology – cyber security and risk management

At a wider level, the political environment remains complex:

- The government continues its negotiation with the EU over Brexit, and future arrangements remain uncertain.
- We will consider your arrangements for managing and reporting your financial resources as part of our work in reaching our Value for Money conclusion.
- We will keep you informed of changes to the financial reporting requirements for 2018/19 through on-going discussions and invitations to our technical update workshops.

Delivering real value through:

- Early advice on technical accounting issues, providing certainty of accounting treatments, future financial planning implications and resulting in draft statements that are 'right first time'
- Knowledge and expertise in all matters local government, including local objections and challenge, where we have an unrivalled depth of expertise.
- Early engagement on issues, especially on ADMs, housing delivery changes, Children services and Adult Social Care restructuring, partnership working with the NHS, inter authority agreements, governance and financial reporting
- Implementation of our recommendations have resulted in demonstrable improvements in your underlying arrangements, for example accounting for unique assets, financial management, reporting and governance, and tax implications for the Cornwall Council companies
- Robust but pragmatic challenge – seeking early liaison on issues, and having the difficult conversations early to ensure a 'no surprises' approach – always doing the right thing
- Providing regional training and networking opportunities for your teams on technical accounting issues and developments and changes to Annual Reporting requirements
- An efficient audit approach, providing tangible benefits, such as releasing finance staff earlier and prompt resolution of issues.

Grant Thornton in Local Government

Our client base and delivery



- We are the largest supplier of external audit services to local government
- We audit over 150 local government clients
- We signed 95% of our local government opinions in 2017/18 by 31 July
- In our latest independent client service review, we consistently score 9/10 or above. Clients value our strong interaction, our local knowledge and wealth of expertise.

Our connections



- We are well connected to MHCLG, the NAO and key local government networks
- We work with CIPFA, Think Tanks and legal firms to develop workshops and good practice
- We have a strong presence across all parts of local government including blue light services
- We provide thought leadership, seminars and training to support our clients and to provide solutions

Our people



- We have over 25 engagement leads accredited by ICAEW, and over 250 public sector specialists
- We provide technical and personal development training
- We employ over 80 Public Sector trainee accountants

Our quality



- Our audit approach complies with the NAO's Code of Audit Practice, and International Standards on Auditing
- We are fully compliant with ethical standards
- Your audit team has passed all quality inspections including QAD and AQRT

Our technical support



- We have specialist leads for Public Sector Audit quality and technical
- We provide national technical guidance on emerging auditing, financial reporting and ethical areas
- Specialist audit software is used to deliver maximum efficiencies

