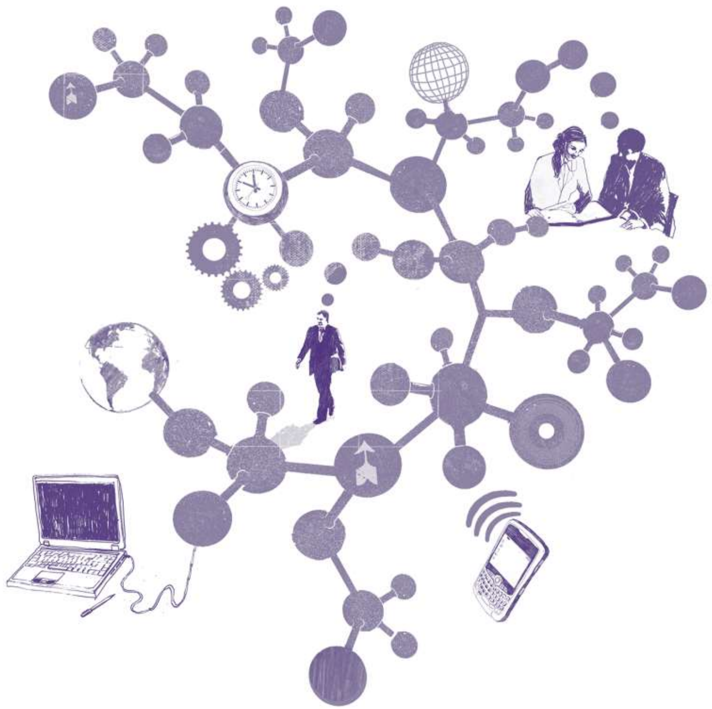
The Annual Audit Letter for Devon County Council

Year ended 31 March 2017

24 October 2017



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Executive summary

Purpose of this letter

Our Annual Audit Letter (Letter) summarises the key findings arising from the work we have carried out at Devon County Council (the Council) for the year ended 31 March 2017.

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

We reported the detailed findings from our audit work to the Council's Audit Committee (as those charged with governance) in our Audit Findings Report on 14 September 2017.

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

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

Our work

Financial statements opinion

We gave an unqualified opinion on the Council's financial statements and those of the Pension Fund hosted by the Council on 21 September 2017.

Value for money conclusion

We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2017. We reflected this in our audit opinion on 21 September 2017.

Whole of government accounts

We completed work on the Council's consolidation return following guidance issued by the NAO and issued an unqualified report on 29 September 2017.

Certificate

We are currently unable to certify that we have completed the audit of the accounts of Devon County Council because we not yet completed work in respect of objections to the 2015/16 and 2016/17 accounts.

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

Grant Thornton UK LLP
October 2017

Audit of the accounts

Our audit approach

Materiality

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

We determined materiality for our audit of the Council's accounts to be £20 million, which is 1.75% of the Council's gross revenue expenditure. We used this benchmark as, in our view, users of the Council's accounts are most interested in how it has spent the income it has raised from taxation and grants during the year.

We also set a lower level of specific materiality of £10,000 for disclosures of officers' remuneration, salary bandings and exit packages and disclosure of auditors' remuneration.

We set a lower threshold of £1 million above which we reported errors to the Audit Committee in our Audit Findings Report.

Devon Pension Fund

For the audit of the Devon Pension Fund accounts, we determined materiality to be £33.724 million, which is 1% of the Fund's net assets. We used this benchmark as, in our view, users of the Pension Fund accounts are most interested in the value of assets available to fund pension benefits.

We set a lower level of specific materiality of £500,000 for management expenses and £25,000 for related party transactions. We set a threshold of £1,959,000 above which we reported errors to the Audit Committee.

The scope of our audit

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

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

We also read the narrative report and annual governance statement to check they are consistent with our understanding of the Council and with the accounts included in the Statement of Accounts on which we gave our opinion.

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

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

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

Audit of the accounts - Council

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
Valuation of pension fund net liability The Council's pension fund net liability, as reflected in its balance sheet, represents a significant estimate in the financial statements.	As part of our audit work we: • Identified the controls put in place by management to ensure that the pension fund net liability was not materially misstated and assessed whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement. • Reviewed the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation. • Gained an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made. • Reviewed the consistency of the pension fund net liability disclosures in notes to the financial statements with the actuarial report from the Council's actuary.	Our audit work involved review of the IAS 19 valuation including the reasonableness of the actuarial assumptions made. The Authority's pension liability was estimated by its own actuaries and we challenged the assumptions underpinning this estimation. Overall, we considered the overall assumptions to be reasonable.

Audit of the accounts – Council (continued)

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of property plant and equipment The Council revalues its assets on a rolling basis over a five year period. The Code requires that the Council ensures that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements.	As part of our audit work we: • Reviewed management's processes and assumptions for the calculation of the estimate. • Reviewed the competence, expertise and objectivity of any management experts used. • Reviewed the instructions issued to valuation experts and the scope of their work. • Held discussions with the Council's valuer about the basis on which the valuation was carried out, challenging the key assumptions. • Reviewed and challenged the information used by the valuer to ensure it was robust and consistent with our understanding. • Tested revaluations made during the year to ensure they were input correctly into the Council's asset register. • Evaluated the assumptions made by management for those assets not revalued during the year to assess how management satisfied themselves that these were not materially different to current value.	The Council revalued a large proportion of its Property, Plant and Equipment in year with a valuation date as at 31 December 2016. The valuation was found to be carried out by a suitably qualified expert. No issues arose from the testing performed. We are satisfied that the Council has demonstrated that the carrying value of all other property, plant and equipment valued in prior years is not materially misstated.

Audit of the accounts – Council (continued)

<table>
<tr><th>Risks identified in our audit plan</th><th>How we responded to the risk</th><th>Findings and conclusions</th></tr>
<tr><td>Changes to the presentation of local authority financial statements
CIPFA has been working on the ‘Telling the Story’ project, for which the aim was to streamline the financial statements and improve accessibility to the user and this has resulted in changes to the 2016/17 CIPFA Code of Practice.

The changes affect the presentation of income and expenditure in the financial statements and associated disclosure notes. A prior period adjustment (PPA) to restate the 2015/16 comparative figures is also required.</td><td>As part of our audit work we:
• Documented and evaluated the process for the recording the required financial reporting changes to the 2016/17 financial statements.
• Reviewed the re-classification of the Comprehensive Income and Expenditure Statement (CIES) comparatives to ensure that they were in line with the Council’s internal reporting structure.
• Reviewed the appropriateness of the revised grouping of entries within the Movement In Reserves Statement (MIRS).
• Tested the classification of income and expenditure for 2016/17 recorded within the Cost of Services section of the CIES.
• Tested the completeness of income and expenditure by reviewing the reconciliation of the CIES to the general ledger.
• Tested the classification of income and expenditure reported within the new Expenditure and Funding Analysis (EFA) note to the financial statements.
• Reviewed the new segmental reporting disclosures within the 2016/17 financial statements to ensure compliance with the CIPFA Code of Practice.</td><td>Our audit work did not identify any significant issues in relation to the risk identified. We confirmed that the disclosures and presentation were in line with what had been reported to the Council in year.

At our request the Expenditure and Funding Analysis (EFA) was included in the notes to the accounts. This was because the CIPFA Code does not define the EFA as a primary statement.</td></tr>
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Audit of the accounts – Pension Fund

This is the risk which had the greatest impact on our overall strategy and where we focused more of our work on the audit of the pension fund.

Risk identified in our audit plan	How we responded to the risk	Findings and conclusions
Valuation of level 3 investments Significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.	As part of our audit work we: • Updated our understanding of your process for valuing Level 3 investments through discussions with relevant personnel. • Performed walkthrough tests of the controls identified in the process. • Tested valuations, on a sample basis, by obtaining and reviewing the audited accounts at latest date for individual investments and agreeing these to the fund manager reports at that date. In addition reconciling those values to the values at 31st March 2017 with reference to known movements in the intervening period. • Reviewed the qualification of the fund managers as experts to value the level 3 investments at year end and gained an understanding of how the valuation of these investments had been reached. • Reviewed the nature and basis of estimated values and considered what assurance management had over the year end valuations provided for these types of investments. • Reviewed the competence, expertise and objectivity of management experts used.	Our audit work did not identify any significant issues in relation to the risk identified.

Audit of the accounts

Audit opinion

We gave an unqualified opinion on the Council's accounts on 21 September 2017, in advance of the 30 September 2017 national deadline.

The Council made the accounts available for audit in line with the agreed timetable, and provided a good set of supporting working papers. The finance team responded promptly and efficiently to our queries during the audit.

Issues arising from the audit of the accounts

We reported the key issues from our audit of the accounts of the Council to the Council's Audit Committee on 14 September 2017.

No significant amendments were made to the Comprehensive Income and Expenditure Statement. However, we did identify one material adjustment where £30m was included in cash and cash equivalents, but should have been included in short term investments.

We identified a control issue in relation to the bank reconciliation at the year end. Due to the early closure of the ledger, the Council amended the way it posted the bank transactions that cleared on the last day of the year. No overall reconciliation of the final amounts in the ledger was completed and the reconciliation did not take into account the total amounts in the ledger of cash and cash equivalents. This led to uncleared suspense account balances which overstated creditors by £2.4m, bank balances by £1.1m and debtor balances by £1.3m. These were amended in the final set of accounts.

Devon Pension Fund accounts

We also reported the key issues from our audit of accounts of the Pension Fund hosted by the Council to the Council's Audit Committee on 14 September 2017 and gave an unqualified opinion on 21 September 2017. No significant issues were identified.

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 with the draft accounts in line with the national deadlines.

Both documents were prepared in line with the relevant guidance and were consistent with the supporting evidence provided by the Council and with our knowledge of the Council.

Whole of Government Accounts (WGA)

We carried out work on the Council's consolidation schedule in line with instructions provided by the NAO . We issued a group assurance certificate which did not identify any issues for the group auditor to consider on 29 September 2017.

Other statutory duties

We also have additional powers and duties under the Act, including powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the accounts and to raise objections received in relation to the accounts.

We received an objection to the 2015/16 accounts in relation to payments to Devon Partnership Trust for delegated responsibilities under the Care Act 2014. Our work is ongoing in relation to this and the estimated fee to date is £15,000. We have also received another objection in relation to the 2016/17 accounts relating to advocacy services provided under the Care Act.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice (the Code), following the guidance issued by the NAO in November 2016 which specified the criterion for auditors to evaluate:

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

Key findings

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

- that recurrent savings would not be identified and achieved to fill the savings gap of £40.6m for 2018/19 to 2020/21;
- that the required savings in year were not achieved resulting in potential overspends for current and future years;
- that the transformational programme will not produce the required level of change and therefore will not deliver the financial savings needed in the required timeframe.

Details of the work we performed and our conclusions are set out on pages 11 to 13.

As part of our Audit Findings report agreed with the Council in September 2017, we agreed recommendations to address our findings. The key recommendation was to introduce a framework with key milestones for monitoring progress of its transformational programme and ensure that it has detailed delivery plans for savings and when they are realistically to be achieved.

Overall VfM conclusion

We are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2017.

Value for Money

Value for money risks

Risk identified in our audit plan	Work carried out	Findings and conclusions
Financial sustainability and identification of recurrent savings for 2017/18 and beyond Whilst the Council has set a balanced budget for 2016/17 and 2017/18, and has increased council tax by the maximum permitted, finding additional savings in future years continues to be a increasing significant challenge. The latest medium term financial strategy (MTFS) outlined that £40.6 m of savings for 2018/19 to 2020/21 still need to be found. To achieve this whilst maintaining provision of service presents a challenge. Following the Budget announcement in March 2017 of increased funding for adult and social care, this may require the Council's medium term financial strategy to be refreshed accordingly. There was a risk that recurrent savings are not identified and achieved to fill the savings gap identified.	We reviewed the Council's arrangements for updating, agreeing and monitoring its Medium Term Financial Strategy. Specifically we considered the robustness of the financial planning assumptions and arrangements for ensuring that financial projections including future savings are realistic and achievable.	The Council's medium term financial strategy for the period 2017/18 to 2020/21 was approved by the Council in February 2017. This includes the savings plans identified to date but also included funding gaps which need be bridged by additional savings plans or increased income. This strategy is supported by a rolling 4 year plan which provides details of individual savings plans and owners and is updated on a regular basis. The 2017/18 budget was supported by significant non-recurrent measures, including the use of reserves. The Council's financial position in future years remains high risk and there are significant and continuing pressures on adult social care. The Council is intending to use the additional precept of £10m per year for adult social care until 2019/20 to help bridge this gap. To address these and the underlying gap the Council must identify and deliver recurrent savings. The Council's plans are reliant on transformational change of services to deliver savings from 2019/20 onwards. Despite the challenges, recent announcements to increase the Better Care Fund (BCF) to fund Adult Social care may ease the burden in the medium term where savings are still to be identified. However as at 31 March 2017, it was unclear how this additional funding is able to be spent and is contingent on agreement with BCF health partners and the specific strategies and targets of the Better Care Fund, which may restrict the use of such funds. As at 31 March 2017, this was still to be determined and it is recommended that the Council revisits its MTFS and budget to take into account this new social care funding, the latest demand for Adult and Children's services and replacement savings which are to be found. Overall, we concluded that the Council had suitable arrangements during the course of the year for managing this risk. However, the Council's financial position remains high risk as at 31 March 2017 and is dependent on delivery of recurrent savings.

Value for Money

Value for money risks (continued)

Risk identified in our audit plan	Work carried out	Findings and conclusions
Delivery of planned recurrent savings The Council set a balanced budget for 2016/17 after identifying £34.3 million of savings that were needed to achieve a balanced budget for the year. To achieve these savings whilst maintaining provision of service presents a challenge. There is a risk of not achieving the required savings in year resulting in potential overspends in budget for current and future years.	We reviewed the arrangements for monitoring and managing delivery of the 2016/17 budget and savings plans. We will review the Council's arrangements for 2017/18 budget setting including identification of savings plans.	Despite the significant pressures on Adult Services which resulted in savings not being achieved, overall the Council delivered its target outturn. Although only £26.8m of the £34.3m planned savings were achieved, regular monitoring has allowed the Council to implement new savings plans and achieve underspends in other areas to ensure the outturn was delivered. The Council monitors its savings plans in year through the budget management group which is attended by Senior Finance Officers. If there are any significant variations, these are reported and escalated to members accordingly. There is clear evidence of this having occurred during the course of the financial year which demonstrates a step forward and progress in terms of reporting variances and budget difficulties. Despite this there is scope to improve the transparency of reporting savings delivery further against planned outcomes. As in previous years, the main budget pressure during the financial year has been on Adult Services where the Council had an overspend of £6.9 million in 2016/17 taking into account a one off benefit of £4m relating to procurement activity and underspend in the Better Care Fund. A total of £7.8m of savings was written out of the plans during the year, however new one off savings of £4m were used to offset this along with the Council achieving underspends in other areas in order to deliver an outturn position as originally forecasted. The non delivery of planned savings has led to the Council revising planned recurrent savings for future years in the latest Medium Term Financial Plan published in February 2017. Relying on compensating in year underspends is only a short term measure and use of one off measures results is increasing financial pressures to deliver more recurrent savings in the future. We have concluded that the risk was sufficiently mitigated and the Council has adequate arrangements in place. However, the non-delivery of some savings in 2016/17 has resulted in increasing pressures going forward.

Value for Money

Value for money risks (continued)

Risk identified in our audit plan	Work carried out	Findings and conclusions
Service transformation projects The Council's has embarked on a programme delivering significant changes to the way in which services are delivered. The programme requires a number of key projects and investments, which are significant both in scale and financial terms. There is a risk that the transformational programme does not produce the required level of change and therefore does not deliver the financial savings needed in the required timeframe.	We reviewed the project management and risk assurance arrangements established by the Council in respect of the transformational programme and related significant projects, to establish how the Council is identifying, managing and monitoring these risks against planned outcomes.	The Council has made some progress in scoping the areas for transformational change, however this remains a significant risk. There still is a lot of work to be done in this area to realise the savings needed. As at 31 March 2017, the transformational plan had not been finalised. Whilst the Council has made arrangements for delivering transformational change in year, methods for monitoring progress were still to be determined and there is a need to agree timelines for delivery. The production of the transformational plan will be a key step and hopefully will assist in the projects progressing at a faster pace, which is needed to deliver the required savings in the medium term. Of the areas identified for transformation, the most advanced is linked to the adult social care which has the most significant budget pressures. The Council has started initial discussions with health partners in parts of the County to collaborate more with the view to change how health and social care for adults is managed and delivered. The Council is planning to scope a number of themes and areas where services require transformation. There is still much to be done to deliver the required transformational programme and savings. In part, reflecting the early stage of the transformational programme, the Council needs to implement more robust arrangements for monitoring and managing the transformational project with timelines agreed. Given the financial pressures, it is imperative that the Council continues to make financial savings in the coming years and the transformational programme is key to this. The Council needs to accelerate the pace of the programme to allow consultation and planning of savings in advance of the required delivery time. It is recommended that the Council has a framework with key milestones for monitoring progress to allow consultation and planning of savings in advance and it has detailed delivery plans for savings required in the medium term and by when. We concluded that the Council was making adequate progress, but there remained more work to do.

Appendix A: Reports issued and fees

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

Fees

	Proposed fee £	Actual fees £	2015/16 fees £
Statutory audit of the Council	105,281	TBC	112,786
Statutory audit of Pension Fund	28,603	28,603	28,603
Total fees (excluding VAT)	**133,884**	**TBC**	**141,389**

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA).

We received an objection to the 2015/16 accounts in relation to payments to Devon Partnership Trust for delegated responsibilities under the Care Act 2014. Our work is ongoing in relation to this and the estimated fee to date is approximately £15,000. We also received another objection in relation to the 2016/17 accounts.

Reports issued

Report	Date issued
Audit Plan	March 2017
Audit Findings Report	September 2017
Annual Audit Letter	October 2017

Fees for other services

Service	Fees £
Audit related services for 2015/16 returns:	
• Certification of Teachers' Pensions end of year return	4,200
• Certification of School Centred Initial Teacher Training return	3,700
• Certification of Local Transport Plan major projects grant return	4,000
Non-audit related services	Nil

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.
- We have considered whether other 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, as reported in our Audit Findings Report.

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