

# The Audit Findings for South Hams District Council

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Year ended 31 March 2019

18 July 2019



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## Appendices

- A. Action plan
- B. Follow up of prior year recommendations
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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 South Hams District Council ('the Council') and the preparation of the Council's financial statements for the year ended 31 March 2019 for those charged with governance.

<p><b>Financial Statements</b></p>	<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 and its 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), 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 was completed on site during June and July. Our findings are summarised on pages 4 to 17. We have not identified any adjustments to the financial statements to date. Audit adjustments are detailed in Appendix C. We have also raised recommendations for management as a result of our audit work in Appendix A. Our follow up of recommendations from the prior year's audit are detailed in Appendix B.</p>	<ul style="list-style-type: none"> <li>- ISA240 assurances from management and those Charged with Governance</li> <li>- Pension Fund assumptions that are related to the pension fund liability figure within the accounts</li> <li>- Pension fund - Mc Cloud issue and review of the actuarial assumptions regarding increase in liability and provision there of</li> <li>- EFA note</li> <li>- Welfare Benefits</li> <li>- Council tax income</li> <li>- NDR income</li> <li>- Grant income</li> <li>- Investments</li> <li>- Cash and cash equivalents</li> <li>- Debtors</li> <li>- Creditors</li> <li>- IFRS9 disclosures. Fair value work from advisers? PWLB loan valuation.</li> <li>- Related parties</li> <li>- REFCUS</li> <li>- Cash flow statement</li> <li>- Valuation of property plant and equipment – particularly evidence from the Council's valuer that indicates detailed consideration regarding any assets not valued in year and a fair value assessment of these and in addition, further evidence to support management's assumptions that assets valued as at 31 December 2019 have not materially altered in value at year end.</li> <li>- Receipt of the valuer's assurance letter to us for the valuation of investment properties held by the Council</li> <li>- Pension assurance letter from the Devon Pension Fund Auditor;</li> <li>- review of the final set of financial statements</li> <li>- Whole of Government accounts certificate.. and</li> <li>- receipt of management representation letter;</li> </ul> <p>We have concluded that the other information to be published with the financial statements is consistent with our knowledge of your organisation and the financial statements we have audited.</p>
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# Summary

## Value for Money arrangements

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').

We have completed our risk based review of the Council's value for money arrangements. We have concluded that South Hams District Council has proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We therefore anticipate issuing an unqualified value for money conclusion. Our findings are summarised on pages 18 to 20.

## Statutory duties

The Local Audit and Accountability Act 2014 ('the Act') also requires us to:

- report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and
- To certify the closure of the audit.

We have not exercised any of our additional statutory powers or duties.

We have completed the majority of work under the Code and expect to be able to certify the completion of the audit when we give our audit opinion.

## 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;
- 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 amended our audit plan, as communicated to you on 10 January 2019 to highlight the risk over the opening balances as we were not the auditors at 31 March 2018. We have also updated our assessment of materiality as set out on page 5.

We have added a further item of review under the Pension Liability risk. That item relates to the emerging issue regarding the increase required in the Pension fund liability amount as a result of the recent Mc Cloud judgement and the government's failure to secure an appeal.

## Conclusion

We have substantially completed our audit of your financial statements and subject to all of the outstanding items listed on page 3 being resolved, we would anticipate issuing an unqualified audit opinion by the 31 July 2019.

## 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 (continued)

### 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.

Our assessment of the value of Materiality has been adjusted to reflect the fact that Gross expenditure is higher than we anticipated at planning. We detail in the table below our assessment of materiality for South Hams District Council.

	Council Amount (£)	Qualitative factors considered
Materiality for the financial statements	967k (planning 1,466k)	<p>We have based our materiality calculation at 1.8% of Gross expenditure on cost of services. For planning purposes we used 1.8% of prior year's Gross expenditure on the Provision of services. We concluded that there were a number of non-expenditure items in notes 9,10 and 11, that we considered should not be taken into account. We have retained 1.8% as an appropriate measure after having taken account of the following factors:</p> <ul style="list-style-type: none"> <li>• The Council operates in a relatively stable, publicly funded business environment;</li> <li>• It's operations are less complex and only a few core business processes are in place; and</li> <li>• the services are all publicly funded.</li> </ul>
Trivial matters	48k (planning 73k)	ISA 260 (UK) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.
Materiality for specific transactions, balances or disclosures		We design our procedures to detect errors in specific accounts at a lower level of precision. We have not identified one disclosure where a separate materiality level is appropriate: Senior Officer remuneration disclosure, where we consider that all pay above £50k will be reviewed.



# Significant findings – audit risks

## Risks identified in our Audit Plan

### 1 The revenue cycle includes fraudulent transactions (rebutted)

Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue.

This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.

We have identified the occurrence and accuracy of Fees, charges & other service income as a significant risk, which was one of the most significant assessed risks of material misstatement and a key audit matter.

Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Council, We have rebutted this presumed risk for the other revenue streams of the Council because:

- there is little incentive to manipulate revenue recognition
- opportunities to manipulate revenue recognition are very limited
- the culture and ethical frameworks of local authorities, including South Hams District Council, mean that all forms of fraud are seen as unacceptable

### 2 Management override of controls

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 Council faces external scrutiny of its spending and this could potentially place management under undue pressure in terms of how they report performance.

We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk, which was one of the most significant assessed risks of material misstatement.

## Commentary

Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Council, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because:

- there is little incentive to manipulate revenue recognition
- opportunities to manipulate revenue recognition are very limited
- The culture and ethical frameworks of local authorities, including South Hams District Council, mean that all forms of fraud are seen as unacceptable

Therefore we do not consider this to be a significant risk for the Council.

We have formally requested specific acknowledgement from officers and members regarding arrangements to identify and detect fraud.

As part of our audit work we have:

- reviewed accounting estimates, judgements and decisions made by management
- tested journal entries
- reviewed unusual significant transactions
- reviewed significant related party transactions outside the normal course of business]

Our audit work so far has not identified any evidence of management over-ride of controls.

We set out later in this section of the report our work and findings on key accounting estimates and judgements.

## Significant findings – audit risks

### Risks identified in our Audit Plan

### Commentary

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#### Valuation of Land and buildings

All material freehold land and buildings which comprise the Authority's property portfolio are revalued by the Council's Valuer on a rolling basis.

Ad hoc valuations take place, for example where assets have been enhanced. In addition, a formal impairment review of the entire holding of land and buildings is undertaken at the end of each financial year, to ensure the carrying value reflects the fair value at the Balance Sheet date

We therefore identified valuation of land and buildings, particularly the annual review, as a significant risk, which was one of the most significant assessed risks of material misstatement.

We have:

- 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;
- discussed with the Council's valuer 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 the revaluations made during the year to ensure they were input correctly into the Council's asset register
- evaluated the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value.

Our work is still ongoing in the area. We await

- a detailed review of the fair value for all assets not valued in year
- receipt of the assurance letter from the valuer on investment properties held by the council, and
- Support for all assumptions used as part of the valuation process for 31 December 2018.

4

#### Valuation of pension fund net liability

The Council'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.

The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£48.6million in the Council's balance sheet) and the sensitivity of the estimate to changes in key assumptions.

We therefore identified valuation of the Council's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement.

We have:

- Identified the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessing 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.
- Undertaken 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 your actuary.

Our detailed work is still ongoing in the area.



## Significant findings - other risks identified

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.

Risks identified in our Audit Plan	Commentary
<p><b>1</b> <b>Completeness of operating expenses</b> The Council is under financial pressure to deliver savings targets. Non-pay expenses represent a significant percentage of the Council's overall operating expenses. Management use judgement to estimate accruals of un-invoiced costs.</p> <p>We identified completeness of non-pay expenses as a risk requiring particular audit attention.</p>	<p>We have</p> <ul style="list-style-type: none"> <li>• documented the processes and key controls over the transaction cycle;</li> <li>• undertaken a walkthrough of the key controls to assess the whether those controls were in line with our understanding;</li> <li>• reviewed estimates, judgements and decisions made by management for unusual and large accruals;</li> <li>• substantively testing of operating expenditure; and</li> <li>• tested the cut-off of expenditure including a review of after date payments to ensure all liabilities had been accounted for in the correct period.</li> </ul> <p>Our work is still ongoing in the area.</p>
<p><b>2</b> <b>Investment property strategy</b> The Council has agreed a commercial property acquisition strategy of up to £60m. The accounting treatment and Funding, principally through long term borrowing, will be a material and unusual transaction in the accounts.</p>	<p>There were no acquisitions during the financial year.</p> <p>We recommend that management continue to monitor emerging guidance from CIPFA and central government on the acquisition of investment properties and related borrowing. In particular, management and members will need to closely scrutinise levels of borrowing related to investment property purchases and ensure that due diligence, legal, financial and other appropriate advice is always sought, and that proportionality is considered as a matter of course for each purchase made.</p>
<p><b>3</b> <b>Allocation of shared costs</b> The Council operates on a shared service basis with West Devon Borough Council. Consequently, there are a number of costs borne by each Council that are reallocated as part of process to allocate costs equitably between the two Councils.</p>	<p>We have:</p> <ul style="list-style-type: none"> <li>• Reviewed the basis of allocation to ensure that it is reasonable and appropriate;</li> <li>• considered any changes from the prior year basis; and</li> <li>• tested the calculation of transferred costs.</li> </ul> <p>Our work is still ongoing in the area.</p>



## Significant findings – key judgements and estimates

Accounting area	Audit Comments	Assessment
<p><b>Provisions for Key estimates and judgements include:</b></p> <ul style="list-style-type: none"> <li>Useful life of PPE</li> <li>Revaluations and impairment of PPE</li> <li>Accruals</li> <li>Provision for NNDR appeals</li> <li>Valuation of pension fund net liability (see page 10)</li> </ul>	<p>We have reviewed the Council's Judgements and estimates and concluded that these are reasonable in respect of the financial statements and the disclosure of financial position of the Council. We would comment as follows:</p> <ul style="list-style-type: none"> <li>We considered the assumptions made by the Council's valuer as reasonable for the Council.</li> <li>The Council's accruals process at year end is appropriate.</li> <li>The estimation of possible NNDR appeals is reasonable.</li> </ul> <p>Our work is still ongoing in the area.</p>	
<p><b>Accounting policies</b></p> <p>Accounting policies were considered for relevance and completeness.</p>	<p>The disclosure of revenue recognition (policy u) did not detail the treatment of material revenue sources.</p>	 Amber
<p><b>Opening balances</b></p> <p>Since the issue of the plan, as we were not the Council's auditors in 2017/18, we have identified that the agreement of opening balances is an audit risk.</p>	<p>We have reviewed the outgoing auditors files, to ensure that we have assurance from their work in 2017/18.</p> <p>We have also reviewed the outcome of significant estimates to ensure that those estimates were reasonably reported.</p> <p>We have verified through existence and rights and obligations testing that the Council's assets were fairly represented at 31 March 2018.</p> <p>Agreed the opening balance to the council's financial system.</p>	 Green

### 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 – key judgements and estimates

	Summary of management's policy	Audit Comments	Assessment																								
<b>Net pension liability – £49m</b>	<p>The Council's total net pension liability at 31 March 2019 is £48.569m (PY £51.459m) comprising the Devon County Council Government pension Fund.</p> <p>The Council uses Barnett Waddingham LLP to provide actuarial valuations of the Council's assets and liabilities derived from these schemes. A full actuarial valuation is required every three years. The latest full actuarial valuation was completed in 2016. A roll forward approach is used in intervening periods, which utilises key assumptions such as life expectancy, discount rates, salary growth and investment returns. Given the significant value of the net pension fund liability, small changes in assumptions can result in significant valuation movements. There has been a £5.848m net actuarial gain/ in 2018/19.</p>	<p>We have;</p> <ul style="list-style-type: none"> <li>Identified the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessing whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement.</li> <li>Reviewed the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation.</li> <li>Undertaken procedures to confirm the reasonableness of the actuarial assumptions made.</li> <li>Reviewed the consistency of the pension fund net liability disclosures in notes to the financial statements with the actuarial report from your actuary.</li> </ul> <p>Our detailed work is still ongoing in the area</p>	<b>Our work is currently ongoing in this area.</b>																								
		<table border="1"> <thead> <tr> <th>Assumption</th> <th>Actuary Value</th> <th>PwC Range</th> <th>Assessment</th> </tr> </thead> <tbody> <tr> <td>Discount rate</td> <td>2.4%</td> <td>2.4% – 2.5%</td> <td>● Green</td> </tr> <tr> <td>Pension increase rate</td> <td>2.4%</td> <td>2.4% - 2.5%</td> <td>● Green</td> </tr> <tr> <td>Salary growth</td> <td>3.9%</td> <td>Dependent on employer</td> <td>● Green</td> </tr> <tr> <td>Life expectancy – males - current age: 45 / 65</td> <td>24.1 / 22.4</td> <td>22.2 – 25.0 / 20.6 – 23.4</td> <td>● Green</td> </tr> <tr> <td>Life expectancy – females - current age : 45 / 65</td> <td>26.2/ 24.4</td> <td>25.0 – 26.6 / 23.2 – 24.8</td> <td>● Green</td> </tr> </tbody> </table>	Assumption	Actuary Value	PwC Range	Assessment	Discount rate	2.4%	2.4% – 2.5%	● Green	Pension increase rate	2.4%	2.4% - 2.5%	● Green	Salary growth	3.9%	Dependent on employer	● Green	Life expectancy – males - current age: 45 / 65	24.1 / 22.4	22.2 – 25.0 / 20.6 – 23.4	● Green	Life expectancy – females - current age : 45 / 65	26.2/ 24.4	25.0 – 26.6 / 23.2 – 24.8	● Green	
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### Assessment

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- 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	Conclusion
<p><b>1</b> <b>Going concern</b></p> <p>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). We will review management's assessment of the going concern assumption and evaluate the disclosures in the financial statements.</p>	<p>Our going concern review has been concluded, and we agree with management that the going concern basis for the preparation of the financial statements is appropriate.</p> <p>The section 151 officer has produced an assessment of the Council's use of the going concern assertion. We have reviewed this and the underlying support and concur with her opinion that the going concern basis is appropriate.</p> <p>In only exceptional circumstances would we expect a local authority not to prepare its accounts on a going concern basis as it requires primary legislation to dissolve a local authority.</p>	<p>The preparation of the financial statements on a going concern basis is appropriate.</p>
<p><b>2</b> <b>CCLA Investment</b></p> <p>In the Statement of Accounts, the Investment of £1.5m is treated as a pooled investment vehicle.</p>	<p>The terms of the agreement allow redemption at cost on demand. The Investment should therefore be included as a short term investment at cost and not re-stated at fair value.</p> <p>Therefore the cumulative write down of value of £23k has been incorrectly charged to the Income and Expenditure account, and the entry should be reversed.</p>	<p>The Investment is incorrectly classified as long term, and has been impaired by £23k.</p> <p>No adjustment has been made in 2018/19.</p>

## 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	Conclusion
<p><b>3</b> <b>Defined Benefit pension Fund</b></p> <p><b>McCloud</b></p> <p>The Court of Appeal has ruled that there was age discrimination in the judges and firefighters pension schemes where there was transitional protections given to scheme members. Refer here for detail.</p> <p>The Government has applied to the Supreme Court for permission to appeal but it will be July (was originally mid-April) before a decision on permission is granted.</p> <p>The legal ruling around age discrimination (McCloud - Court of Appeal) also has implications for other pension schemes where they have implemented transitional arrangements on changing benefits.</p> <p><b>GMP</b></p> <p>The High court ruled that defined benefit pension schemes must remove any discriminatory effect that guaranteed minimum pension (GMP) entitlements have had on member benefits</p>	<p>The impact on South Hams District Council is assessed by the actuary to be an increased liability of £851k.</p> <p>A review performed by the NAO and specialist actuarial reviews on a national basis has concluded that there is a requirement for a provision to be made in the accounts. We concur with this view as the event has occurred, a reasonable estimate can be made and the pension liability should be increased.</p> <p>A note outlining the potential effect has been added to the accounts to aid understanding.</p> <p>The Actuarial valuation for the Council has assumed that that the Fund will pay limited increases for members that have reached State pension age by 6 April 2016, with the Government providing the remainder of the inflationary increase.</p> <p>We continue to perform further work and review on the assumptions made by the actuary regarding both the Mc Cloud estimate and the GMP values.</p>	<p>The value is close to materiality, we would expect the financial statements to reflect the estimated impact. We recommend that management amend the accounts to reflect the increase in the pension liability as a result of the recent Mc Cloud ruling.</p> <p>Management have decided not to amend for this. We will require specific representation from those charged with governance should it be agreed that the amendment should not be made.</p> <p>Currently this is shown as an unadjusted error in Appendix 3.</p>

## 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 Committee. We have not been made aware of any incidents in the period and no other issues have been identified during the course of our audit. We will update our understanding of management's arrangements at the Committee.
2 <b>Matters in relation to related parties</b>	We are not aware of any significant incidences of non-compliance with relevant laws and regulations.
3 <b>Matters in relation to laws and regulations</b>	We are not aware of any significant incidences of non-compliance with relevant laws and regulations.
4 <b>Written representations</b>	A standard letter of representation has been requested from the Council.
5 <b>Confirmation requests from third parties</b>	We requested from management permission to send confirmation requests for Bank and Investment balances. This permission was granted and the requests were sent. Some confirmations are still outstanding. We also requested assurances over the audit of the Devon County Pension Fund from the Fund's auditors, these have not yet been received.
6 <b>Disclosures</b>	Our review found no material omissions in the financial statements. We have agreed some minor disclosure amendments, which management have included in the final statements.





## 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 Statement of Accounts, 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>We have nothing to report in this regard.</p>
② <b>Matters on which we report by exception</b>	<p>We have not identified any issues we would be required to report by exception in the following 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 information of which we are aware from our audit</li> <li>• The information in the Narrative Report is materially inconsistent with the information in the audited financial statements or our knowledge of the Council acquired in the course of performing our audit, or otherwise misleading.</li> </ul> <p>We have nothing to report in this regard.</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>We will submit our certificate on Whole of Government Accounts, following the signing of the financial statements.</p>
④ <b>Certification of the closure of the audit</b>	<p>We intend to certify the closure of the 2018/19 audit of South Hams District Council in our audit opinion.</p>

## Internal controls

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
 Green	No internal control weaknesses have been identified	
 Amber	IT General Controls have been reviewed. There are a number of identified weaknesses that have been the subject of a separate report.	Agreed with management as part of a separate report which is on the agenda. No issues highlighted in that report had an impact upon our audit approach.

### Assessment

-  Significant deficiency – risk of significant misstatement
-  Deficiency – risk of inconsequential misstatement

"The purpose of an audit is for the auditor to express an opinion on the financial statements.

Our audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control.

The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance." (ISA (UK&I) 265)

# Value for Money

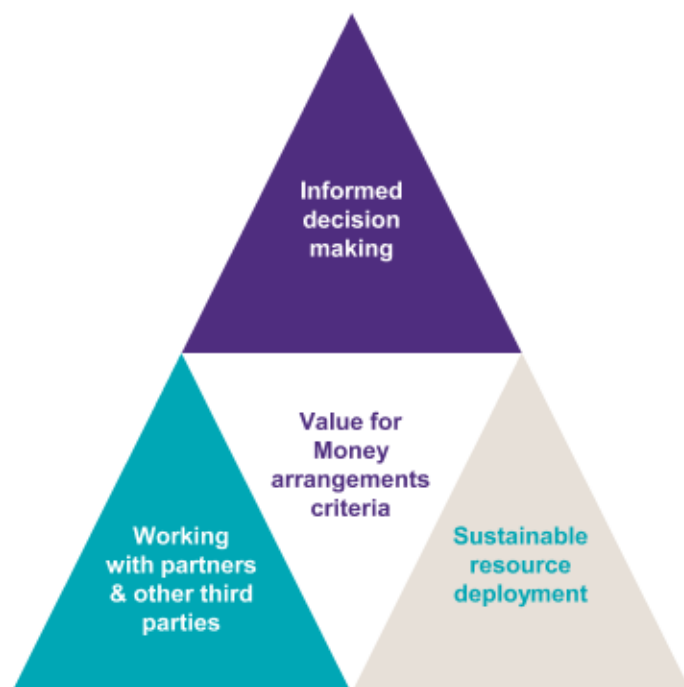
## Background to our VFM approach

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 one 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 16 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.

The risk identified in the audit plans set out below:



### Informed decision making

At the end of September 2018 The Council was forecasting an overspend of £66,000 (0.7% of the total Budget £8.983 million) for 2018/19.

However, the Council has identified some financial challenges over the life of its Medium Term Financial Strategy. The cumulative budget gap is forecast to be £1.8 million by 2023/24, assuming annual savings are not achieved.

The Council has recently let its Waste collection contract jointly with West Devon Borough Council, which is predicted to achieve £0.4 million of the savings required.

The Council plans to address this through a challenging programme that includes:

- Budget delivery and reserves management;
- Commercial development opportunities within the South Hams District and associated borrowing

The Council has identified a key risk that may arise that would affect its achievement. Some of the councils identified savings are part of its joint working with West Devon Borough Council, e.g. the award of a joint waste collection service and the continuation of joint provision of services.

We carried out further work only in respect of the significant risks we identified from our initial and ongoing risk assessment. Where our consideration of the significant risks determined that arrangements were not operating effectively, we have used the examples of proper arrangements from AGN 03 to explain the gaps in proper arrangements that we have reported in our VFM conclusion.

# 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:

- The Council's out-turn for 2018/19 and delivery of the Budget;
- The MTFS for 2019/20 to 2023/24,
- The Council's plans to address its forecast budget gap, including the letting of the waste contract, it's approach to Commercialisation and joint working with West Devon Borough Council.

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 page 16.

## Overall conclusion

Based on the work we performed 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.

## Recommendations for improvement

We discussed findings arising from our work with management and have made no recommendations for the Council.

## 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
<p><b>1</b> At the end of September 2018 The Council was forecasting an overspend of £66,000 (0.7% of the total Budget £8.983 million) for 2018/19.</p> <p>However, the Council has identified some financial challenges over the life of its Medium Term Financial Strategy. The cumulative budget gap is forecast to be £1.8 million by 2023/24, assuming annual savings are not achieved.</p> <p>The Council has recently let its Waste collection contract jointly with West Devon Borough Council, which is predicted to achieve £0.4 million of the savings required.</p> <p>The Council plans to address this through a challenging programme that includes:</p> <ul style="list-style-type: none"> <li>• Budget delivery and reserves management;</li> <li>• Commercial development opportunities within the South Hams District and associated borrowing</li> </ul> <p>The Council has identified a key risk that may arise that would affect its achievement. Some of the councils identified savings are part of its joint working with West Devon Borough Council, e.g. the award of a joint waste collection service and the continuation of joint provision of services.</p>	<p>The council made a small surplus in 2018/19 of £0.049m after statutory accounting adjustments. This puts the Council in a good position at 31 March 2019. General Fund usable reserves stand at £15.191k, General Fund Balance of £1.898m and earmarked reserves of £13.293m, following the release of £13.477m of Business rates retention provisions.</p> <p>In the Council's Medium Term Financial Strategy for 2019/20 to 2023/24 the Council has identified a £0.638m shortfall in resources for 2019/20, rising to an annual shortfall of £1.83m by 2023/24. The Council is progressing various options for closing the budget gap in 2019/20 and future years.</p> <p>The waste services contract, was let in conjunction with West Devon BC, for 2019/20. The Council has been presented with informed reports as part of the decision making process, it has had the opportunity to challenge the presented reports prior to making its decisions. We would therefore conclude that, in the case of the waste services procurement the Council has been informed at the key stages of the decision making process and that the current arrangements in place at this time are sound.</p> <p>The Council had not purchased any Investment property as part of the strategy, by 31 March 2019. However, The Council's commercial property strategy has been approved by Council. No properties had been purchased by the year end. The strategy sets out an intention to acquire Investments for economic regeneration objectives within its economic area.</p> <p>The council has sought advice, produced an Investment strategy and sought appropriate approval. Going forward each project will require individual approval by the Council</p>	<p><b>Auditor view</b></p> <p>The council has recognised the need for immediate and large scale actions and has already let its Waste Contract which is projected to achieve annual savings of approximately £0.4m. The Council has approved its Commercial Investment Strategy, which provides a net income stream to the Council as an ancillary benefit. Other projects being considered are Pension strategy to reduce the annual "past service deficit contributions", and a review of the use of the Council's assets and operational plan savings review.</p> <p>We recommend that management continue to monitor emerging guidance from CIPFA and central government on the acquisition of investment properties and related borrowing. In particular, management and members will need to closely scrutinise levels of borrowing related to investment property purchases and ensure that due diligence, legal, financial and other appropriate advice is sought, proportionality is considered prior to further purchases.</p> <p><b>Management response</b></p> <p>An updated budget report was presented to the Executive on 18th July 2019 predicting a budget gap of £0.45 million for 2020/21 and an aggregated Budget Gap of £2.2 million to 2024/25. Section 7 of the report set out the various options for closing the budget gap. The Council is awaiting the announcement of the Spending Review for 2019 from the Government.</p>



## 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. No Non-audit services have been identified



	Fees £	Threats identified	Safeguards
<b>Audit related</b>			
None			
<b>Non-audit related</b>			
None			

# Action plan

We have identified 2 of 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 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	 IT General Controls have been reviewed. There are a number of identified weaknesses that have been the subject of a separate report.	<p>Agreed with management as part of a separate report.</p> <p><b>Management response</b> See separate report.</p>
2	 The Council has agreed a commercial property acquisition strategy of up to £60m. The accounting treatment and Funding, principally through long term borrowing, will be a material and unusual transaction in the accounts.	<p>We recommend that management continue to monitor emerging guidance from CIPFA and central government on the acquisition of investment properties and related borrowing. In particular, management and members will need to closely scrutinise levels of borrowing related to investment property purchases and ensure that due diligence, legal, financial and other appropriate advice is sought, proportionality is considered prior to further purchases.</p> <p><b>Management response</b> The Council agrees with the recommendation and will continue to monitor any new guidance and to seek the appropriate assurances through the due diligence undertaken on each acquisition. The Council has set an overall borrowing limit of £60million based on proportionality and this will be annually reviewed by Members as part of the Council's Medium Term Financial Strategy.</p>

#### Controls

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

## Follow up of prior year recommendations

The Council's previous auditors identified the following issue in the audit of South Hams District Council Council's 2017/18 financial statements, which resulted in one recommendation being reported in the 2017/18 Audit Findings report.

	Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
1		<p>It was noted that the reconciliation of national non-domestic rates cash and refunds were not being performed in a reasonable time frame, and that some reconciling items were not being cleared in a timely fashion.</p> <p><b>Management response</b></p> <p>The recommendation is agreed. This has already been addressed and monthly reconciliations are being submitted to the Finance community of Practice Lead for approval.</p>	<p>No further issues have been identified in 2018/19.</p>

### Assessment

- ✓ Action completed
- X Not yet addressed

# Audit Adjustments

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 None identified	0	0	0

## 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?
Notes 10 and 11	Detail in the note does not reconcile to the disclosure in the CI&ES.	Notes should be amended to agree with CI&ES disclosure	<b>Yes</b>
		<b>Management response</b> This has been adjusted for 2018-19 to show the net position rather than the gross position.	
Note 23	Draft note included an adjustment for Proceeds on Capital Disposals of £7,269k. The disclosure included the proceeds from disposal of investments	Note should be amended	<b>Yes</b>
Hyperlinks	The statement accounts should not contain hyperlinks to other documents or websites. This is because these then become part of the statement of accounts are covered by the Statement of responsibilities and the audit opinion, and as such would require additional audit work.	Hyperlinks should be replaced by narrative description of any supporting information.	

# Audit Adjustments

## 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 Audit 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 Impact of the McCloud judgement on the IAS 19 liability in the accounts.				
Remeasurement of the net defined benefit liability	851			
MiRS note 7 – Reversal of items relating to retirement benefits debited or credited to the CIES	-851		0	
Pension liability		-851		
Pensions Reserve		851		
2 CCLA Investment	23	23	23	Trivial
	<b>23</b>	<b>23</b>	<b>23</b>	



## Fees

We confirm below our final fees charged for the audit

### Audit Fees

		Proposed fee	Final fee
<b>Council Audit</b>		33,421	33,421
<b>Additional audit fees for additional work required by the regulator</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 will be considering the impact on the financial statements along with any audit reporting requirements.	-	1,500
Pensions – IAS19	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. As part of our audit, we identified discrepancies between the pension fund gross asset valuation in the authority's accounts compared to the Pension Fund statements (of Devon County Council). The authority has obtained an updated report from its actuary, which we are in the process of reviewing.	-	1,500
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.	-	1,500
<b>Total audit fee</b>			<b>37,921</b>

### Non Audit Fees

Fees for other services	Fees £'000
None	



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