

# The Audit Findings for East Sussex County Council

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**Year ended 31 March 2019**

**12 July 2019**



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

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# Headlines

This table summarises the key findings and other matters arising from the statutory audit of East Sussex County Council ('the Council') for the year ended 31 March 2019 for those charged with governance.

<b>Financial Statements</b>	<p>Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Council's financial statements:</p> <ul style="list-style-type: none"><li>• give a true and fair view of the financial position of the Council 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 and Pension Fund Financial Statements), 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 the following pages. We have not identified any adjustments to the financial statements which would result in an adjustment to the Council's Comprehensive Income and Expenditure Statement. Audit adjustments in relation to disclosure errors are detailed in Appendix B. We have raised recommendations for management as a result of our audit work in Appendix A. One of these recommendations has been classified as a significant risk and is in regards to management carrying out a review of who has General Ledger (SAP) access providing virtually full system rights</p> <p>Our work is substantially complete and there are no matters of which we are aware that would require modification of our audit opinion or material changes to the financial statements, subject to the following outstanding matters;</p> <ul style="list-style-type: none"><li>• review of supporting documentation for indexation and revaluation of property plant and equipment (PPE);</li><li>• receipt and review of supporting documentation for PPE additions, debtors, fees and charges, operating expenses, leases and journals sampled items;</li><li>• final internal quality review ;</li><li>• receipt of the management representation letter; and</li><li>• review of the final set of financial statements.</li></ul> <p>Pending adjustments agreed with management we 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> <p>Our anticipated audit report opinion will be unqualified.</p>
<b>Value for Money arrangements</b>	<p>Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report if, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion').</p>	<p>We have completed our risk based review of the Council's value for money arrangements. We have concluded that East Sussex County Council has proper arrangements to secure economy, efficiency and effectiveness in its use of resources.</p> <p>We therefore anticipate issuing an unqualified value for money conclusion. Our findings are summarised later in this report</p>

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# Headlines (Continued)

This table summarises the key findings and other matters arising from the statutory audit of East Sussex County Council ('the Council') for the year ended 31 March 2019 for those charged with governance.

<b>Statutory duties</b>	<p>The Local Audit and Accountability Act 2014 ('the Act') also requires us to:</p> <ul style="list-style-type: none"><li>• report to you if we have applied any of the additional powers and duties ascribed to us under the Act; and</li><li>• To certify the closure of the audit.</li></ul>	<p>We have not exercised any of our additional powers or duties.</p> <p>We have completed the majority of work under the Code but we cannot formally conclude the audit and issue our completion certificate until:</p> <ul style="list-style-type: none"><li>• we have issued our report on the consistency of the pension fund financial statements; and</li><li>• we have completed the work necessary to issue our whole government Accounts assurance statement</li></ul>
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## Acknowledgements

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

# Summary

## Overview of the scope of our audit

- This Audit Findings Report presents the observations arising from the audit that are significant to the responsibility of those charged with governance (the Governance Committee) to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Our engagement has been with the Audit Committee, who review and scrutinise the financial statements and makes recommendations to the Governance Committee. We have discussed our audit findings with management and the Audit Committee.
- 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 your business and is risk based, and included:

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

We have not had to alter or change our audit plan, as communicated to you on 25 March 2019, except for revising planning materiality which was based on your prior year gross expenditure. Our revised materiality figure is £15m which equates to approximately 1.75% of your gross expenditure in 2018/19.

## Conclusion

We have substantially completed our audit of your financial statements and subject to the outstanding matters listed on page 3 being resolved, we anticipate issuing an unqualified audit opinion.

## 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.

	Council Amount (£)
Materiality for the financial statements	15m
Performance materiality	10.5m
Trivial matters	0.75m

# Audit findings – Significant risks

In our Audit Plan we set out our identification of significant risks. The following pages highlight the audit outcome against those significant risks.

Risks identified in our Audit Plan	Commentary
<p><b>1 Improper revenue recognition</b></p> <p>We have considered the rebuttable presumed risk under ISA (UK) 240 that revenue may be misstated due to the improper recognition of revenue.</p> <p>Having considered the risk factors set out in ISA (UK) 240 and the nature of the revenue streams at the Council we have rebutted this presumed risk for revenue streams which are derived from Council Tax, Business Rates and Grants on the basis that they are income streams that are hard to manipulate.</p> <p>We have not deemed it appropriate to rebut this presumed risk for all other material streams which are as follows:</p> <ul style="list-style-type: none"> <li>• Fees, charges and other service income</li> <li>• Support services recharges (support services charges removed from income in 2018-19, therefore no longer a revenue stream)</li> </ul>	<p><b>Auditor commentary</b></p> <p>Fees, charges and other service income - summary of work performed and audit findings.</p> <ul style="list-style-type: none"> <li>• We reviewed and evaluated your accounting policy for recognition of income for appropriateness and compliance with the LG Code of Practice;</li> <li>• We reviewed and sample tested this income to supporting documentation;</li> <li>• We reviewed and challenged significant estimates and judgements made by management.</li> </ul> <p>Subject to satisfactory resolution of matters identified on page 3, our audit work has not identified any issues in respect of revenue recognition.</p>
<p><b>2 Management override of controls</b></p> <p>Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entries.</p>	<p><b>Auditor commentary</b></p> <p>Summary of work performed and audit findings.</p> <ul style="list-style-type: none"> <li>• We evaluated the design effectiveness of management controls over journals;</li> <li>• We obtained a full listing of journal entries which was then analysed to identify and test high risk unusual journals;</li> <li>• We tested unusual journals recorded during the year and post year end for appropriateness and corroboration.</li> <li>• We considered the reasonableness of significant accounting estimates and critical judgements made by management;</li> <li>• We evaluated the rationale for any changes in accounting policies or significant transactions.</li> </ul> <p>We identified journal entries being prepared and recorded with no descriptions, increasing the potential for erroneous or fraudulent posting to go unnoticed. We have raised a recommendation in this regard, see Appendix A for more detail. Subject to final internal review our audit work has not identified any other issues in respect of management override of controls.</p>

# Audit findings – Significant risks

## Risks identified in our Audit Plan

## Commentary

### 3 Valuation of Property, Plant and Equipment

You revalue your land and buildings on an rolling three-year basis to ensure that carrying value is not materially different from current value. This represents a significant estimate by management in the financial statements.

Additionally, management will need to ensure the carrying value of assets not revalued as at 31 March 2019 in the financial statements is not materially different from the current value at the financial statements date.

We identified the valuation of land and buildings revaluations and impairments as a risk requiring special audit consideration.

### Auditor commentary

Summary of work performed and audit findings

- We reviewed and evaluated management's processes and assumptions for the calculation of the estimate, the instructions issued to valuation experts and the scope of their work.
- We considered the competence, expertise and objectivity of your management expert (valuer).
- We discussed with the valuer the basis on which the valuation is carried out and challenged their key assumptions.
- We reviewed the information used by the valuer to ensure it is robust and consistent with our understanding.
- We tested revaluations made during the year to ensure they have been input correctly into the Council's asset register.
- We evaluated the assumption made by management for those assets that were revalued during the year using management's indexation approach.
- We evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value.

Subject to the outstanding items listed on page 3, our audit work has not identified any issues in respect of the valuation of property, plant and equipment. See page 9 for more analysis of your indexation.

### 4 Valuation of pension fund net liability

Your Pension Fund net liability, as reflected in your balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements

We identified valuation of the your Pension Fund net liability as a risk requiring special audit consideration.

### Auditor commentary

Summary of work performed and audit findings

- We identified the controls put in place by management to ensure that the pension fund liability is not materially misstated. We also assessed whether these controls were implemented as expected
- We evaluated the competence, expertise and objectivity of the actuary who carried out your pension fund valuation. We gained an understanding of the basis on which the valuation is carried out
- We undertook procedures to confirm the reasonableness of the actuarial assumptions by using our own auditor's expert.
- We checked the consistency of the pension fund asset and liability disclosures in notes to the financial statements with the actuarial report from your actuary

Subject to final internal review our audit work has not identified any issues in respect of valuation of the pension fund net liability.

# Audit findings – Significant risks

Risks identified in our Audit Plan		Commentary
5	<b>Private Finance Initiative (PFI) liability</b>	<b>Auditor commentary</b>
	<p>You have two builds which are financed through PFI schemes: Waste and Peacehaven Schools. As these PFI transactions are significant, complex and involve a degree of subjectivity in the measurement of financial information we have categorised them as a significant risk.</p>	<p>Summary of work performed and audit findings</p> <ul style="list-style-type: none"><li>• We reviewed your PFI models and assumptions contained therein;</li><li>• We reviewed and tested the output produced by your PFI models to generate the financial balances within the financial statements;</li><li>• We reviewed your PFI disclosures to ensure they are consistent with the Code of Practice on Local Authority Accounting and the International Accountancy Standard IFRIC12.</li></ul> <p>Subject to final internal review, our audit work has not identified any issues in respect of valuation of the pension fund net liability.</p>



# Audit findings - other issues

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

Issue	Commentary	Auditor view
<p><b>1 Potential Impact of the McCloud judgement</b></p> <p>The Court of Appeal has ruled that there was age discrimination in the judges and firefighters pension schemes where transitional protections were given to scheme members.</p> <p>The expectation is that this ruling will apply to other schemes where transitional protections were given to scheme members, including the Local Government Pension Scheme.</p> <p>The Government applied to the Supreme Court for permission to appeal this ruling, but permission to appeal was unsuccessful. The case will now be remitted back to an employment tribunal for remedy.</p>	<p>Discussion is ongoing in the sector regarding the potential impact of the ruling on the financial statements of Local Government bodies.</p> <p>Management requested an estimate from the Council's actuary of the potential impact of the McCloud ruling. The actuary's estimate was of a possible increase in pension liabilities of £6,627k, and an increase in service costs for the 2019/20 year of £1,085k.</p> <p>Management's view is that the impact of the ruling is not material for East Sussex County Council, and will be considered for future years' actuarial valuations. The accounts presented for members' approval do not include an adjustment for this matter.</p>	<p>We have reviewed the analysis performed by the actuary, and consider that the approach taken to arrive at this estimate is reasonable.</p> <p>Although we are of the view that there is sufficient evidence to indicate that a liability is probable, we note the amount involved is not material. We also acknowledge the significant uncertainties relating to the estimation of the impact on the Council's liability.</p> <p>We have included this as an uncertainty and an unadjusted error within Appendix B.</p>
<p><b>2 Valuation of Property, Plant and Equipment – Indexation approach</b></p> <p>For any assets not formally valued by the external valuer management applied an indexation to the remaining assets.</p> <p>The valuation of land and buildings revaluations and impairments as a risk requiring special audit consideration.</p>	<p>Following a review of your 2017/18 financial statements performed by our technical team, management were challenged over the use of indices in valuation. Dating back to 2015/16 CIPFA have queried the use of indices in the valuation of non-current assets indicating indices should only be used by appropriate valuation experts in support of their professional judgement.</p> <p>Management approached their external valuer to include a judgement within the valuation report regarding the appropriateness of their approach and whether it would be reasonable to expect the average percentage change across the group of revalued assets to apply to that whole group.</p> <p>The valuer confirmed the Council's approach is reasonable.</p>	<p><b>Auditor view</b></p> <p>We reviewed management's indexation approach for the calculation of the estimate.</p> <p>We evaluated the assumptions made by management for those assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value.</p> <p>We discussed with the valuer management's approach to challenge the appropriateness of the estimation.</p> <p>The working papers were provided on 28 June 2019, at the date of this draft the work is currently ongoing.</p>



# Audit findings – key judgements and estimates

	Summary of management's policy	Audit Comments	Assessment																								
<b>Net pension liability – £472.6m</b>	<p>You recognise and disclose your retirement benefit obligation in accordance with the measurement and presentational requirement of IAS 19 'Employee Benefits'.</p> <p>Your net pension liability at 31 March 2019 is £473.6m (2018: 409.8m) comprising the East Sussex County Council Local Government pension scheme. You engage Hymans Robertson LLP to provide actuarial valuations of your assets and liabilities derived from (this scheme). 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 £35.8m net actuarial loss during 2018/19.</p>	<ul style="list-style-type: none"> <li>We have assessed your actuary, Hymans Robertson LLP, to be competent, capable and objective.</li> <li>We have reviewed the 2018/19 roll forward calculation carried out by the actuary and have no issues to raise.</li> <li>We have used an auditor's expert to assess the actuary and assumptions made by your actuary – see table below for our comparison of actuarial assumptions:</li> </ul> <table> <tr> <th>Assumption</th><th>Actuary Value</th><th>Auditor's expert comments</th><th>Assessment</th></tr> <tr> <td>Discount rate</td><td>2.40%-2.50%</td><td>Assumption is reasonable but towards the more optimistic end of expected ranges</td><td>●</td></tr> <tr> <td>Pension increase rate</td><td>2.50%-2.40%</td><td>Assumption sits towards the middle, slightly towards the higher, more prudent end of expected ranges</td><td>●</td></tr> <tr> <td>Salary growth</td><td>1.00% to 2020</td><td>In line with public sector pay caps</td><td>●</td></tr> <tr> <td>Life expectancy – Males currently aged 45 / 65</td><td>Pensioners: 21.5-22.8 Non-pensioners: 23.7-24.4</td><td>Assumption is based on the CMI 2013 model and allowance is towards more prudent end of expect ranges</td><td>●</td></tr> <tr> <td>Life expectancy – Females currently aged 45 / 65</td><td>Pensioners: 24.1-25.1 Non-pensioners: 26.2-26.9</td><td>Assumption is based on the CMI 2013 model and allowance is towards more prudent end of expect ranges</td><td>●</td></tr> </table>	Assumption	Actuary Value	Auditor's expert comments	Assessment	Discount rate	2.40%-2.50%	Assumption is reasonable but towards the more optimistic end of expected ranges	●	Pension increase rate	2.50%-2.40%	Assumption sits towards the middle, slightly towards the higher, more prudent end of expected ranges	●	Salary growth	1.00% to 2020	In line with public sector pay caps	●	Life expectancy – Males currently aged 45 / 65	Pensioners: 21.5-22.8 Non-pensioners: 23.7-24.4	Assumption is based on the CMI 2013 model and allowance is towards more prudent end of expect ranges	●	Life expectancy – Females currently aged 45 / 65	Pensioners: 24.1-25.1 Non-pensioners: 26.2-26.9	Assumption is based on the CMI 2013 model and allowance is towards more prudent end of expect ranges	●	●
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## 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

# Audit findings – key judgements and estimates

	Summary of management's policy	Audit Comments	Assessment
<b>Level 3 investments</b>	You have investment properties that are valued on the balance sheet as at 31 March 2019 at £18m. In order to determine this value, management engaged Montagu Evans to complete the valuation of properties as at 31 March 2019. The value of the investment has increased by £2.7m in 2018/19.	<ul style="list-style-type: none"> <li>We have assessed your valuer, Montagu Evans, to be competent, capable and objective.</li> <li>We have carried out completeness and accuracy testing of the underlying information provided to the valuer used to determine the estimate and have no issues to report.</li> <li>The valuation method remains consistent with the prior year.</li> </ul>	
<b>Going concern</b>	Your accounts have been prepared on the going concern basis. Public sector bodies are assumed to be going concerns where the continuation of the provision of a service in the future is anticipated, as evidenced by inclusion of financial provision for that service in published documents.	<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).</p> <p>We have subjected the 2019/20 budget and Medium Term Financial Plan (MTFP) to 2021/22 to detailed scrutiny, and reviewed the planned savings proposals for 2019/20 and 2020/21 in our consideration of the appropriateness of management's use of the going concern assumption.</p> <p>In 2019/20 you need to make savings of £5.1m. We have carried out work on your financial sustainability (see value for money work) and concluded your financial planning is robust and your current reserves position provides an appropriate level of flexibility.</p> <p>We have not identified any material uncertainty in relation to your ability to continue as a going concern.</p>	

## 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 and key assumptions to be reasonable

# 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>	<ul style="list-style-type: none"> <li>We have previously discussed the risk of fraud with management and Audit Committee. We have not been made aware of any significant incidents in the period and no issues have been identified during the course of our audit procedures.</li> </ul>
2	<b>Matters in relation to related parties</b>	<ul style="list-style-type: none"> <li>We are not aware of any related parties or related party transactions which have not been disclosed.</li> </ul>
3	<b>Matters in relation to laws and regulations</b>	<ul style="list-style-type: none"> <li>You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any such incidences from our audit work.</li> </ul>
4	<b>Written representations</b>	<ul style="list-style-type: none"> <li>A letter of representation has been requested.</li> </ul>
5	<b>Confirmation requests from third parties</b>	<ul style="list-style-type: none"> <li>We requested from management permission to send confirmation requests in respect of your bank, investments and loans balances. This permission was granted and the requests were sent. All of these requests were returned with positive confirmation, with the exception of confirmations requested in respect of investments held with Barclays and Goldman Sachs. We are continuing to chase these confirmations requests with assistance from your officers and in the meanwhile will undertake alternative procedures to verify whether these balances are materially fairly stated as at 31 March 2019.</li> </ul>
6	<b>Disclosures</b>	<ul style="list-style-type: none"> <li>Our review found no material omissions in your financial statements. We identified a number of immaterial disclosure adjustments which are set out later within this report.</li> </ul>
7	<b>Audit evidence and explanations/significant difficulties</b>	<ul style="list-style-type: none"> <li>Except for the outstanding items noted on page 3, all information and explanations requested from management was provided.</li> </ul>

# Other responsibilities under the Code

Issue	Commentary
<b>1 Other information</b>	<ul style="list-style-type: none"> <li>We are required to give an opinion on whether the other information published together with your audited financial statements (including the Annual Governance Statement, Narrative Report and Pension Fund Financial Statements), is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.</li> </ul> <p>The narrative report is balanced and largely covers the expected content as per the Code of Practice. A potential area for future improvement is a reporting of performance or a relevant cross reference to show achievement against corporate objectives.</p> <p>Pending receipt of an updated version of the Narrative Report with agreed amendments we plan to issue an unmodified opinion in this regard.</p>
<b>2 Matters on which we report by exception</b>	<p>We are required to report on a number of matters by exception in a numbers of areas:</p> <ul style="list-style-type: none"> <li>If the Annual Governance Statement (AGS) does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the other information of which we are aware from our audit</li> <li>If we have applied any of our statutory powers or duties</li> </ul> <p>Pending receipt of an updated version of the AGS with agreed amendments we have nothing to report on these matters.</p>
<b>3 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> <ul style="list-style-type: none"> <li>Note that work detailed work is not required as the Council does not exceed the threshold. We will issue a return to the NAO to confirm.</li> </ul>
<b>4 Certification of the closure of the audit</b>	<p>We intend to certify the closure of the 2018/19 audit of East Sussex County Council with the audit opinion.</p>

# Value for Money

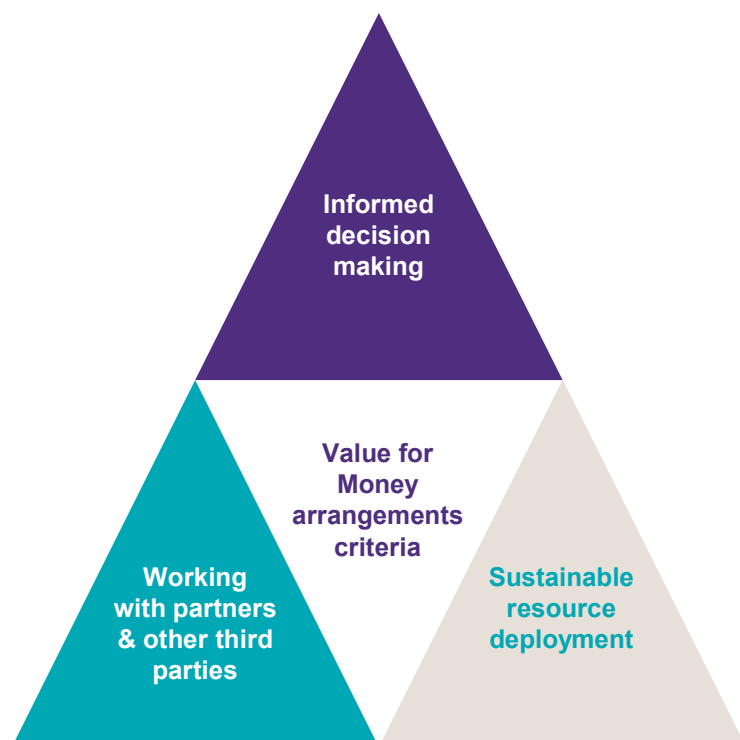
## Background to our VFM approach

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

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

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

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



## Risk assessment

We carried out an initial risk assessment in February 2019 and identified three 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 25 March 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.

## 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 work we have undertaken against the three areas we highlighted to you in our Audit Plan:

- Ongoing Financial Sustainability
- Working in partnership with the NHS
- Brexit

We have set out more detail including the conclusions we drew from this work on the next few pages.

## 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.

# Value for Money

## Overview

In response to challenging financial conditions and the need to continue to deliver priority services, the Council has developed a 'Core Offer'. This is an articulation of the minimum outcomes a competent and efficient Council would expect to provide by 2020/21, in the context of agreed local priorities and the resources available over the next three years. The Medium Term Financial Plan has been developed to align with and support the delivery of services as defined by the Core Offer. We note that the Core Offer represents a level of service that is less than has been the case in the past, but is still considerably above the level of a minimum statutory service.

In our view the Council has managed a challenging financial position effectively in 2018/19 and in doing so has demonstrated robust financial management arrangements. The Council faces a significant challenge over the next few years to address a structural deficit of expenditure over income. This will require the realisation of £12.3m of planned savings, in addition to a further £14m of new savings to close the projected funding gap up to 2021/22. This means the successful delivery of £26.3m of savings in total over the 3 year MTFP period which is approximately 6% of the 2018/19 net cost of services (equivalent to a 2% average reduction in spend each year). This is in addition to £129m that has already been taken out of the Council budget between 2010 and 2019.

To support them in achieving this the Council has set aside reserves to help manage risk, centred around Strategic Reserves of £32.4m at the end of 2018/19 (equivalent to 7.6% of the net cost of services of £424.4m). In addition to a budgeted contingency of £3.5m in each year, the available reserves should enable the Council to continue to maintain a balanced budget throughout the MTFP period, while the remaining funding gap is closed, even if there is slippage in the realisation of savings.

The Council is working with partners across Sussex to integrate health and social care, to reduce costs and improve services for residents. It has undertaken preparations for Brexit which are aimed at mitigating any actual or perceived risk.

## Financial performance 2018/19

The Council reported a financial outturn for the year ending 31 March 2019 as an underspend on budget of £8m. The surplus has enabled a net increase in reserves, to be allocated to the Capital Programme (£4.6m) and to increase the financial management reserve (£3.4m) which is set aside to help the Council manage future financial risks.

The Quarter 4 Outturn report to Cabinet reports that within this position, there was an overspend on demand-led social care services of £4.1m (Adult Social Care - £1.1m and Children's Services - £3.0m). This overspend was partly offset by underspends across other departments (notably £2.2m from waste, transport concessions and the Orbis partnership).

The remaining overspend was covered, and a surplus generated by a number of other one off benefits including over-performance on Treasury Management partly due to slippage on the capital programme reducing borrowing costs (£4.6m), under-spends on other centrally held budgets (£0.3m), and one off benefit through the government's release of surplus on the national Business Rates Levy (£1.4m). The overall underspend was further increased by the release of the general contingency budget of £3.5m, which was not required. This is set aside each year to manage financial risks and to help protect reserves.

- We note that the Adult Social Care delivered a relatively small overspend (£1.1m, less than 1% of the net cost of the service) with the assistance of additional funding from the social care precept, enhanced better care fund and other additional funding. The overspend was attributed to increasing demand for and cost of services for older people and working age adults.
- The 2018/19 outturn indicates that there may be higher than anticipated cost pressures in the Children's budget that may be structural and linked to problems in the local care market. The overspend was attributed to agency costs for Looked after Children with complex needs, increased costs of private sector accommodation for vulnerable families and the level and cost of high cost care placements.
- We note that while there was some slippage on the Capital programme, 92% of the budgeted capital expenditure was delivered in the period which indicated relatively robust planning and control.

**The Council will have to make sure that structural demand pressures in Children's and Adult Social Care manifesting as budget overspends, are adequately factored into the MTFP in future years as recurrent increases in costs, mitigated through service transformation.**



# Value for Money

## Financial planning (MTFP) 2019/20 to 2021/22

The Council has a robust, detailed and comprehensive financial planning process and has a demonstrable track record of delivery. Each year the State of the County report is undertaken to take stock of the County, the needs and priorities of residents. In 2018, the Council drew on this to develop and consult on a 'Core Offer' proposition that set out how the Council would reconfigure services to deliver its 4 priority outcomes within the available financial resources (driving sustainable economic growth, keeping vulnerable people safe, helping people help themselves and making best use of resources). The Council's Reconciling Policy, Performance and Resources (RPPR) process then matched available resources with delivery plans for these priority outcomes. Resource limits are set for each service that reflect these outcomes and the resources available to deliver them and a Medium Term Financial Plan (MTFP) was developed.

The Council's current MTFP projects a funding gap that builds to £14m by the end of 2021/22. This assumes that £12.3m of planned savings will be successfully delivered in the period. The £14m gap equates to a further 4% reduction in the net cost of services over three years. This remains challenging and it is important that the momentum for change established with the development of the core offer is maintained and financial control remains robust.

**It is likely that the Council and its elected members will need to make some difficult choices about service provision in order to restore a balanced financial position and it will be important to maintain an effective dialogue with residents as the Council moves towards the Core Offer.**

The Council has taken a relatively prudent approach to its financial planning assumptions that underpin this position. Overall, the assumptions appear to be reasonable based on the available information and the approach taken by other councils. Key assumptions include:

- Council tax is assumed to increase by 2.99% in 2019/20. Future increases are subject to a new council decision each year but the MTFP does allow for growth in Council tax receipts over the period.
- The Council will be taking part in the governments 75% Business Rates retention pilot, and business rate projections have been adjusted to reflect this in the early years of the MTFP. The assumptions for growth thereafter are relatively flat, reflecting the prevailing economic conditions and infrastructure in East Sussex.
- As part of this pilot, Revenue Support Grant will reduce from 2019/20.
- The allowable Adult Social Care precept increase was taken in full by 2018/19 and the MTFP assumes no further increases in future years.

- For 2018/19 and 2019/20 the government has allocated additional funding for social care directly through the better care fund. We note that government have yet to confirm that funding will continue at this level for the medium term, and the Council has taken a cautious approach in assuming that cost pressures will re-emerge if this is withdrawn.
- Key cost pressures factored into the position include pay awards, contract price inflation and demand pressures particularly in adults and children's social care.

These assumptions are broadly in line with what we would expect to see, based on our knowledge of other councils.

## Financial governance - savings plans

The Council has a good track record of planning and delivering savings plans, including the successful management of slippage. The Council's future financial sustainability depends on the successful delivery of its savings programme. In the revised MTFP published in February 2019 to accompany the 2019/20 budget, the Council set out an ambitious plan that front-loaded a savings requirement of £17m for 2018/19, leaving £5.1m in 2019/20, £5.2m in 2020/21 and £2m for 2021/22. This reflected revisions from the original MTFP set in January 2018.

In 2018/19 total planned savings were £18.9m (£17m planned in the MTFP and £1.8m of benefit carried forward from 2017/18). During 2018/19 £9.9m of planned savings were reported as successfully delivered in year (green rated), with a further £9m that incurred slippage so that the planned benefit was not taken in 2018/19 (amber rated). The temporary shortfall in year was compensated by £7.3m of additional one-off savings and the use of £1.6m of reserves. These measures enabled the Council to make the net contribution to reserves of £8m in year. The Council can therefore demonstrate success in managing planned savings targets in 2018/19.

The main areas of slippage in the savings programme were Adult Social Care (£6.1m) and Children's Social Care (£2.6m). In both cases, the savings are reported as on track to deliver the full benefit in 2019/20.



# Value for Money

Detailed savings proposals arising from the RPPR process and the move to the Core Offer were provided to Cabinet for Review and approval in November 2018 and January 2019.

**We note that the Council incurred slippage in its ambitious savings programme for 2018/19. This was successfully managed enabling the overall plan to be delivered and demonstrating agile financial management. The Council should continue to monitor and manage slippage in the savings plan and unplanned budget pressures which could indicate that savings are not embedded.**

## Financial governance – monitoring

Each department holds its own departmental weekly monitoring meeting and issues are escalated to the weekly CMT meeting. Savings are RAG rated, in terms of on track to achieve (Green), plans that are on track but where the timetable has slipped (Amber), and those savings which have not or are unlikely to be delivered (Red). Where there is slippage in the savings plan, departments are required to provide alternative plans to enable them to deliver within their control total.

There are quarterly financial reports to Cabinet and each department provides a detailed commentary. Finance and performance information is reported together, as this gives a more rounded view. Savings plan delivery is also separately monitored as part of the Quarterly reporting to Cabinet (on a formal basis) providing significant transparency on progress.

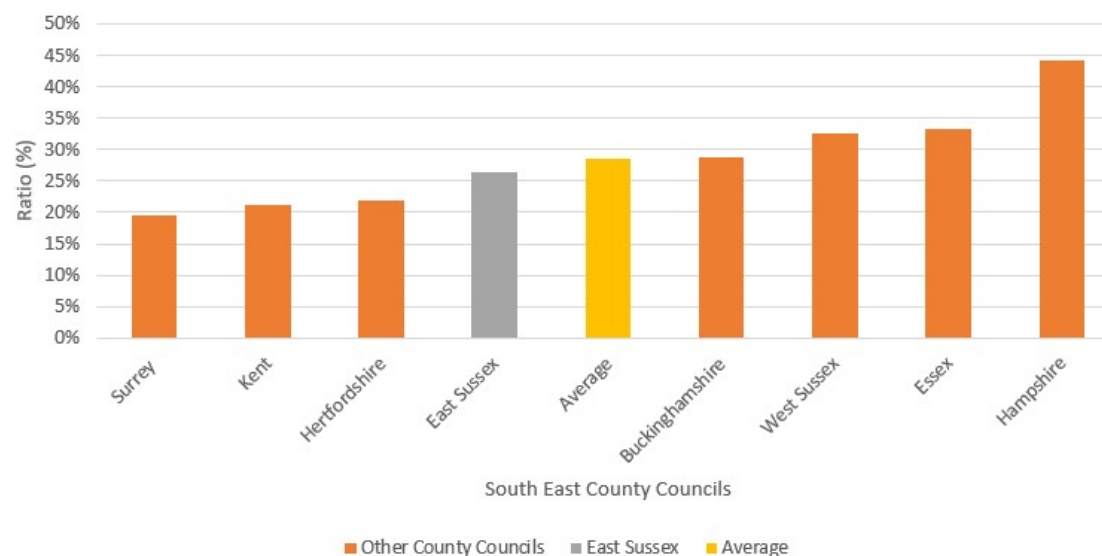
## Reserves

The Council has sufficient reserves available to manage the projected financial deficits over the MTFP period up to 2023. Total usable reserves as at 31 March 2019 were £112.4m (excluding schools) of which £32.4m is held in Strategic Reserves available to help sustain the Councils financial position during transition to the Core Offer. The Strategic Reserves are equivalent to 7.6% of the net cost of services in 2018/19.

Your reserve levels as a percentage of your expenditure are comparable to the average for County Councils in the region (see graph below).

There are currently sufficient Strategic Reserves to continue to cover the current projected deficit up to 2021/22 (£14m) and any slippage in planned savings benefits over the same period (£12.3m). However, the Council rightly recognises that failure to address the underlying deficit over the MTFP period could lead to the inability to set a balanced budget in future years.

General fund and earmarked general fund reserves (excluding schools)  
as a percentage of net service revenue expenditure



# Value for Money

## Working in partnership with the NHS

The Council's partnership working arrangements with the NHS are longstanding and successful. There are challenges in relation to the financial environment however financial plans appear to be on track across the system as at month 2. Health and social care services are being integrated via the East Sussex Better Together programme and collectively, partners in the local health and social care economy are now designing the next phase of this plan as well as looking to the wider Integrated Care System (ICS) across Sussex. The planned merger of the seven Sussex Clinical Commissioning Groups (CCGs) into three CCGs has the aim of supporting further integration.

The East Sussex Better Together (ESBT) programme began in August 2014. ESBT is a partnership between East Sussex County Council, Eastbourne, Hailsham & Seaford CCG and Hastings & Rother CCG and the NHS providers.

ESBT's aims are to improve - healthy living and wellbeing, proactive care, crisis intervention and admissions avoidance, bedded care, discharge to assess and maintaining independence. The methodology that has been used to work towards these aims are to integrate services across the council, CCGs and East Sussex Healthcare Trust. Data is shared across organisations to better understand the relationships and impacts of each organisation rather than each working in a silo. Integration takes the form of joint commissioning and delivery of services. ESBT reports successful outcomes, for example during the time the programme has been operational, growth in demand for acute care has been significantly lower compared to the regional and national average. The aim is to redistribute care from hospitals to the community by focusing on early intervention to prevent conditions getting to an advanced state where patients need to be hospitalised.

Connecting 4 You is a similar programme which aims to improve local health and social care for the population of High Weald, Lewes and the Havens.

Going forward, both programmes are set to be combined into one, with the council working with all three CCGs and the Trust to bring together health and social care services across East Sussex in the form of the East Sussex Transformation Plan 2019/20. Governance arrangements have been put in place to support this new initiative, in the form of the Chief Finance Officers Group (Chaired by the Council's Director of Adult Social Care) and the East Sussex Health and Social Care Executive Group.

Both groups have representatives from across the healthcare organisations and the council. Ultimately the groups report to the East Sussex Health and Wellbeing Board. Reports are also taken to Council.

One of the challenges to integration is the difficult financial environment surrounding the NHS organisations in Sussex, with most organisations being in a deficit position. Financial plans and assumptions have been shared and drawn up together, called the 'East Sussex 3+2 Plan'. The plan aims to deliver financial sustainability within three years. The monthly Chief Finance Officers Group covers system risk, including monitoring individual entity and system savings plans. Quarter 1 reports disclose that the plan is on track to deliver for 2019/20. There is a risk that the NHS organisations slip into financial difficulty later in the year which could affect support and delivery of the programme. In 2018/19 you, like most councils in England, overspent against your Adult Social Care budget. Management recognise that the transformation of the delivery of adult social care via integration with NHS bodies must continue apace to move towards making these services sustainable in future. Your focus in this regard in East Sussex is commendable.

Going forward High Weald Lewes Havens, Eastbourne, Hailsham and Seaford, and Hastings and Rother CCGs are likely to merge, creating a single CCG co-terminus with the council in East Sussex with a population of just over 800,000. Plans are being drawn up over the summer to develop a longer-term Health & Social Care programme for East Sussex which encapsulates the requirements of the emerging Primary Care Networks (PCNs) and Integrated Care System (ICS). Plans are being designed to significantly increase productivity and use available funding more efficiently by managing people in the community, responding more quickly to people in crisis in their own homes, and facilitating a speedier discharge from hospital.

# Value for Money

## Brexit

You have been closely linked to the Government's Brexit plans via your Chief Executive, who is the lead for the South East Hub. You are part of Local Resilience Forums, which include blue light services, including the East Sussex Emergencies and Resilience Partnership, the Sussex Resilience Forum (SRF) the and the London and South East Local Resilience Forums.

Work has been undertaken at the National, Regional and Local level to plan and prepare for a No Deal and/or disorderly EU-Exit with the aim of reducing and mitigating the impact to residents and businesses in East Sussex.

You have asked each of your departments to consider how they may be affected by Brexit and to put in place contingency plans to deal with any potential or perceived risk. Six half-day Tactical Awareness Training workshops were delivered by the SRF to ensure stakeholders are as prepared as possible to operate at the tactical level should a multi-agency response be required.

You have modelled for a 'no deal' Brexit scenario, and identified areas where it is sensible to put plans in place. New plans for East Sussex are in relation to Newhaven Port, waste collection and disposal, fuel supply, service delivery, communication (internally and externally) and your supply chain. The highest risk has been identified as road congestion caused by traffic needing access to Newhaven port. You are a partner in the Newhaven Port Emergency Plan meetings along with Sussex Police and Highways England which aim to identify and mitigate any adverse effects on Newhaven Port and the town.

Following the announcement that Article 50 has been extended until 31 October 2019, Central Government's no-deal contingency operations have been stood down and consequently you are taking a proportionate approach to avoid unnecessary impact on your usual business. You are taking part in a multi-agency SRF debrief to identify lessons learnt and where appropriate to revise plans. You have reported your approach to Brexit internally to the Corporate Management Team and to the Audit Committee.

## Impact of Brexit and other risks on finances

The Council has taken steps to develop resilience in the MTFP to manage uncertainties and risks. This underpins the MTFP assumptions and is evident in the development of the budget through the RRPR process over the period November to January. For example, the initial worst case deficit was projected to be £45.7m up to 2021/22, before being mitigated through the adoption of the Core Offer proposals and other funding adjustments.

The impact of Brexit has been considered and the RPPR report notes risks associated with the national economy, the duties the Government expects the Council to carry out and the workforce available to both the Council and the service providers in the Care Sector. Management is aware that as the details of any deal and the practical realities begin to emerge these will need to be taken into account in financial planning.

The Council's response to Brexit and the arrangements you have in place seem reasonable.

# 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

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 C

## **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 were identified.

# 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		<ul style="list-style-type: none"> <li><b>Access to client maintenance functionalities (SCC4) (SAP access providing virtually full system rights)</b></li> </ul> <p>13 users with firefighter ID's have access to using SCC4. Improper execution of client administration transactions could result in a loss of entire client (SAP system), including information, data and configured functionalities.</p>	<p>The profile should be reserved for use within an emergency and the number of firefighter type ID should be monitored with access being regularly reviewed.</p> <p><b>Management response</b></p> <p>A review of the number of users with firefighter ID's has been performed and as of June there are 7 users, this will be monitored (update provided by Taina Tate, Senior Security Consultant).</p>
2		<ul style="list-style-type: none"> <li><b>Journals with no descriptions</b></li> </ul> <p>We identified journal entries being prepared and recorded with no descriptions, increasing the potential for erroneous or fraudulent posting to go unnoticed.</p>	<p>Management should consider running exception reports to identify and review journal entries with no narrative included.</p> <p><b>Management response</b></p> <p>An email will be circulated to all users as a reminder. This was recently pick up also as part of a recent internal audit review.</p>

## Controls

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

# 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

There were no adjusted misstatements for the year ending 31 March 2019.

## Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which are due to be made in the final set of financial statements.

Disclosure omission	Detail	Adjustment agreed?
<b>Prior period adjustment</b>	<ul style="list-style-type: none"> <li>A disclosure note should be included which summaries the adjustment/reallocation made to the prior year CIES categories. It should include all impacted accounts, the amount before the restatement and provide an explanation to why the statement was required.</li> </ul>	✓
<b>Critical judgements</b>	<ul style="list-style-type: none"> <li>Critical judgements should be clarified as to what judgement is being made in each case.</li> </ul>	✓
<b>Note 6c EFA</b>	<ul style="list-style-type: none"> <li>In part c of this note, the total income for 2018/19 has been cast incorrectly (should show as £886,644k). The analysis of total income and total expenditure for 2017/18 and 2018/19 should agree back to the CIES</li> </ul>	✓
<b>Note 20 Financial instruments</b>	<ul style="list-style-type: none"> <li>There should be a note that shows how the 2018 comparatives under the old classification have been reclassified into the new categorisations. Items should be reconciled to their category on the balance sheet. Financial asset fair values table should be consistent with the fair value hierarchy table.</li> </ul>	✓
<b>Note 26 Usable reserves</b>	<ul style="list-style-type: none"> <li>The in year opening balance adjustment to the 2018 figure should be shown and a note included to state why an adjustment is required (IFRS 9 impairment allowance).</li> </ul>	✓
<b>Note 39 Related parties</b>	<ul style="list-style-type: none"> <li>The transactions with East Sussex Pension Fund should be included in this note.</li> </ul>	✓
<b>Various</b>	<ul style="list-style-type: none"> <li>Various other minor disclosure changes, including adjustments to correct signage in notes 13, 23 and 32.</li> </ul>	✓

# 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
<p><b>1 Potential impact of the McCloud judgement</b></p> <p>The legal ruling around age discrimination (McCloud - Court of Appeal) has implications for pension schemes where transitional arrangements on changing benefits have been implemented.</p> <p>Discussion is ongoing in the sector regarding the potential impact of the ruling on the financial statements of Local Government bodies.</p> <p>The Council has requested an estimate from its actuary of the potential impact of the McCloud ruling. The actuary's estimate was of a possible increase in pension liabilities of £6,627k, and an increase in service costs for the 2019/20 year of £1,085k.</p> <p>We have satisfied ourselves that there is not a risk of material error as a result of this issue. We also acknowledge the significant uncertainties relating to the estimation of the impact on the Council's liability.</p>	6,627	(6,627)	6,627	<p>The figures provided by the actuary are an estimate, and not a formal actuarial valuation.</p> <p>Although we are of the view that there is sufficient evidence to indicate that a liability is probable, we are satisfied that the differences are not likely to be material.</p> <p>This issue will be considered as part of the next actuarial valuation exercise in 2019/20.</p>
<b>Overall impact</b>	<b>£6,627</b>	<b>£(6,627)</b>	<b>£6,627</b>	

# Fees

We confirm below our final fees charged for the audit, which are in line with the fee set out by PSAA. There were no fees for the provision of non audit services.

## Audit Fees

	Proposed fee	Final fee
Council Audit	64,350	64,350
Total audit fees (excluding VAT)	£64,350	£64,350

## Non Audit Fees

There have been no non-audit fees or audited related services undertaken for the Council.



