



The Annual Audit Letter for East Sussex County Council

Year ended 31 March 2019

October 2019



Contents



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Executive Summary

Purpose

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at East Sussex County Council (the Council) for the year ended 31 March 2019.

This Letter is intended to provide a commentary on the results of our work to the Council and external stakeholders, and to highlight issues we wish to draw to the attention of the public. In preparing this Letter, we have followed the National Audit Office (NAO)'s Code of Audit Practice and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'. We reported the detailed findings from our audit work to the Council's Audit Committee in our Audit Findings Report on 12 July 2019.

Our work

Respective responsibilities

We have carried out our audit in accordance with the NAO's Code of Audit Practice, which reflects the requirements of the Local Audit and Accountability Act 2014 (the Act). Our key responsibilities are to:

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

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

Materiality	We determined materiality for the audit of the Council's financial statements to be £15m, which is approximately 2% of the Council's gross revenue expenditure.
Financial Statements opinion	We gave an unqualified opinion on the Council's financial statements on 20 September 2019.
Whole of Government Accounts (WGA)	We completed work on the Council's consolidation return following guidance issued by the NAO.
Use of statutory powers	We did not identify any matters which required us to exercise our additional statutory powers.
Value for Money arrangements	We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources. We reflected this in our audit findings report to the Council on 12 July 2019.
Certificate	We certified that we completed the audit of the financial statements of East Sussex County Council in accordance with the requirements of the Code of Audit Practice on 20 September 2019.

Audit of the Financial Statements

Our audit approach

Materiality

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

We determined materiality for the audit of the Council's financial statements to be £15m, which is approximately 2% of the Council's gross revenue expenditure. We used this benchmark as, in our view, users of the Council's financial statements are most interested in where the Council has spent its revenue in the year.

We set a lower threshold of £750,000, above which we reported errors to the Audit Committee in our Audit Findings Report.

The scope of our audit

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

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

We also read the remainder of the financial statements, the narrative report and the annual governance statement to check their consistency with our understanding of the Council and with the financial statements on which we gave our opinion.

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

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

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

Audit of the Financial Statements

Significant Audit Risks

These are the significant risks which had the greatest impact on our overall strategy and where we focused more of our work.

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Improper revenue recognition</p> <p>We 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 revenue streams at the Council we 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 did not deem it appropriate to rebut this presumed risk for fees, charges and other service income.</p>	<ul style="list-style-type: none"> • We reviewed and evaluated the Council's accounting policy for recognition of income for appropriateness and compliance with the Local Government Accounting Code of Practice; • We reviewed and sample tested fees, charges and other service income income to supporting documentation; • We reviewed and challenged significant estimates and judgements made by management. 	<p>Our audit work did not identify any issues.</p>
<p>Management override of internal controls</p> <p>Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entries.</p>	<ul style="list-style-type: none"> • We evaluated the design effectiveness of management controls over journals; • We obtained a full listing of journal entries which was then analysed to identify high risk unusual journals; • We tested unusual journals recorded during the year and post year end for appropriateness and corroboration; • We considered the reasonableness of significant accounting estimates and critical judgements made by management; • We evaluated the rationale for any changes in accounting policies or significant transactions. 	<p>We identified journal entries being prepared and recorded with no descriptions, increasing the potential for erroneous or fraudulent posting to go unnoticed. We raised a recommendation in this regard.</p> <p>Our audit work did not identify any other issues.</p>

Audit of the Financial Statements

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Valuation of Property, Plant and Equipment</p> <p>The Council revalues land and buildings on an rolling three-year basis. The valuation of property, plant and equipment at the balance sheet date represents a significant estimate by management in the financial statements.</p> <p>We identified the valuation of land and buildings revaluations as a risk requiring special audit consideration.</p>	<ul style="list-style-type: none"> • 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 management’s 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 had been input correctly into the Council’s asset register; • We evaluated the assumptions 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 had satisfied themselves that these were not materially different to current value. 	<p>Our audit work did not identify any issues.</p>

Audit of the Financial Statements

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Valuation of pension net liability The Local Government Pension Scheme net liability represents a significant estimate in the financial statements</p> <p>We identified valuation of the pension net liability as a risk requiring special audit consideration</p>	<ul style="list-style-type: none"> • We identified the controls put in place by management to ensure 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 the 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 the actuary. 	<p>We found the pension net liability to be materially misstated due to the Council using an estimated rate of return on assets provided by its actuary. The Council obtained a revised actuarial report and the financial statements were adjusted to show the actual return on assets, which increased the net liability.</p> <p>Our audit work did not identify any other issues.</p>
<p>Private Finance Initiative (PFI) liability The Council has two builds which are financed through PFI schemes: Waste and Peacehaven School.</p> <p>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>	<ul style="list-style-type: none"> • We reviewed the Council's PFI models and assumptions contained therein; • We reviewed and tested the output produced by the PFI models to generate the financial balances within the financial statements; • We reviewed the PFI disclosures to ensure they are consistent with the Code of Practice on Local Authority Accounting and the International Accountancy Standard IFRIC12. 	<p>Our audit work did not identify any issues.</p>

Audit of the Financial Statements

Pension Fund Significant Audit Risks

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

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Valuation of level 3 investments</p> <p>Under ISA 315 significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.</p> <p>We therefore identified the valuation of level 3 investments as a significant risk.</p>	<ul style="list-style-type: none"> • We gained an understanding of management's process for valuing Level 3 investments and evaluating the design of the associated controls; • We reviewed the nature and basis of estimated Level 3 valuations and considered what assurance management has over the year end valuations provided for these investments; • For a sample of investments, we tested the valuation by obtaining and reviewing the audited accounts as at 31 December 2018 for individual investments and agreeing these to fund manager reports at that date and reconciling those values to the valuations reported at 31 March 2019 with reference to known movements in the intervening period. 	<p>Our audit work did not identify any issues.</p>

Audit of the Financial Statements

Audit opinion

We gave an unqualified opinion on the Council's financial statements on 20 September 2019.

Preparation of the financial statements

The Council presented us with draft financial statements in accordance with the national deadline. We were provided with a good set of working papers although not all were available at the start of the audit in early June. The finance team responded promptly to our queries during the course of the audit however there were delays in receiving appropriate supporting evidence from the wider organisation.

Issues arising from the audit of the financial statements

We reported the key issues from our audit to the Council's Audit Committee on 12 July 2019 and updated the Audit Committee on 13 September 2019.

Annual Governance Statement and Narrative Report

We are required to review the Council's Annual Governance Statement and Narrative Report. It published them on its website in line with the national deadlines.

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

Pension fund accounts

We gave an unqualified opinion on the pension fund accounts on 20 September 2019. We reported the key issues from our audit of the pension fund accounts to the Council's Audit Committee on 12 July 2019.

Whole of Government Accounts (WGA)

We carried out work on the Council's Data Collection Tool in line with instructions provided by the NAO . We issued an assurance statement which did not identify any issues for the group auditor to consider on 20 September 2019.

Other statutory powers

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

Certificate of closure of the audit

We certified that we have completed the audit of the financial statements of East Sussex County Council in accordance with the requirements of the Code of Audit Practice on 20 September 2019.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice, following the guidance issued by the NAO in November 2017 which specified the criterion for auditors to evaluate:

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

Key findings

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

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

As part of our Audit Findings report agreed with the Council in 12 July 2019, we agreed recommendations to address our findings.

Overall Value for Money conclusion

We are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2019.

Value for Money conclusion

Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>Financial sustainability Rising demand for the Council's services and falling government grants are putting the Council's finances under considerable strain. The Council needs to manage its resources carefully to ensure a sustainable future.</p>	<p>We carried out a detailed review of the Council's Medium Term Financial Plan, including savings plans, financial governance (monitoring of finances) and reserve levels.</p>	<p>No issues noted – we concluded the Council had the processes and procedures in place to secure economy, efficiency and effectiveness in its use of resources.</p>
<p>Working in partnership with the NHS Failure to secure maximum value from partnership working with the NHS could impact negatively on social care and public health services, leading to worse health outcomes for residents and also increased current and future costs.</p>	<p>As part of our work we reviewed documentation and spoke to officers at the Council and NHS partners to understand the Council's significant NHS collaboration initiatives, including East Sussex Better Together and Connecting 4 You, as well as plans for the future.</p>	<p>No issues noted – we concluded the Council had the processes and procedures in place to secure economy, efficiency and effectiveness in its use of resources.</p>
<p>Brexit With the UK due to leave the European Union on 29 March 2019, there will be national and local implications for which you will need to plan.</p>	<p>As part of our work we reviewed the Council's arrangements and plans relating to Brexit. Our review focussed on areas such as workforce planning, supply chain analysis and impact on finances.</p>	<p>No issues noted – we concluded the Council had the processes and procedures in place to secure economy, efficiency and effectiveness in its use of resources.</p>

A. Reports issued and fees

We confirm below our final reports issued and fees charged for the audit and confirm there were no fees for the provision of non audit services.

Reports issued

Report	Month issued
Audit Plan	March 2019
Audit Findings Report	July 2019
Annual Audit Letter	October 2019

Fees – external audit

	Planned £	Actual fees £	2016/17 fees £
Statutory audit of the Council	64,350	80,350	83,572
Audit of Pension Fund	20,487	25,487	26,607
Total fees	84,837	105,837	110,179

Fees – grant certification

	Planned £	Actual fees £	2016/17 fees £
Teachers' Pension grant certification	4,200	TBC	Unknown
Total fees	4,200	TBC	

Audit fee variation

As outlined in our audit plan, the 2018-19 scale fee published by PSAA of £64,350 for the County and £20,487 for the Pension Fund assumes that the scope of the audit does not significantly change. There are a number of areas where the scope of the audit has changed, which has led to additional work. These are set out in a table on the next page.

Fee variations are subject to PSAA approval.

A. Reports issued and fees

Council area	Reason	Fee proposed
Assessing the impact of the McCloud ruling	The Government's transitional arrangements for pensions were ruled discriminatory by the Court of Appeal last December. The Supreme Court refused the Government's application for permission to appeal this ruling. As part of our audit we reviewed the revised actuarial assessment of the impact on the financial statements along with any audit reporting requirements.	£3,000
Pensions – IAS 19	The Financial Reporting Council has highlighted that the quality of work by audit firms in respect of IAS 19 needs to improve across local government audits. Accordingly, we have increased the level of scope and coverage in respect of IAS 19 this year to reflect this fact. We carried out additional work to address the material error in the draft financial statements in relation to the return on pension assets.	£3,000
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. In addition, the use of a second valuer report, late working papers and lack of clarity about which items had been revalued led to further work being required. We have increased the volume and scope of our audit work to reflect these factors.	£5,000
Audit overruns	We have discussed with officers, a number of areas where we had to apply additional resources to deliver the audit. These include, but are not limited to; transaction listings with multiple 'ins and outs' lengthening the process to select a sample which reflected the year end balance; time consuming reconciliations between transaction listings received at interim and those at year end; and response delays to audit queries arising from sample testing.	£5,000
Total		£16,000

Pension Fund area	Reason	Fee proposed
IAS19 letters	We were asked to provide IAS19 letters for a number of local authority auditors which caused us additional work.	£5,000
Total		£5,000

Our commitment to our local government clients

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

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

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

New opportunities and challenges for your community

The Local Government economy

Local authorities face unprecedented challenges including:

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

At a wider level, the political environment remains complex:

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

Delivering real value through:

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

Grant Thornton in Local Government

Our client base and delivery



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

Our connections



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

Our people



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

Our quality



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

Our technical support



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



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