

The Annual Audit Letter for Warwickshire County Council

DRAFT

This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report.

Year ended 31 March 2016

October 2016

Grant Patterson

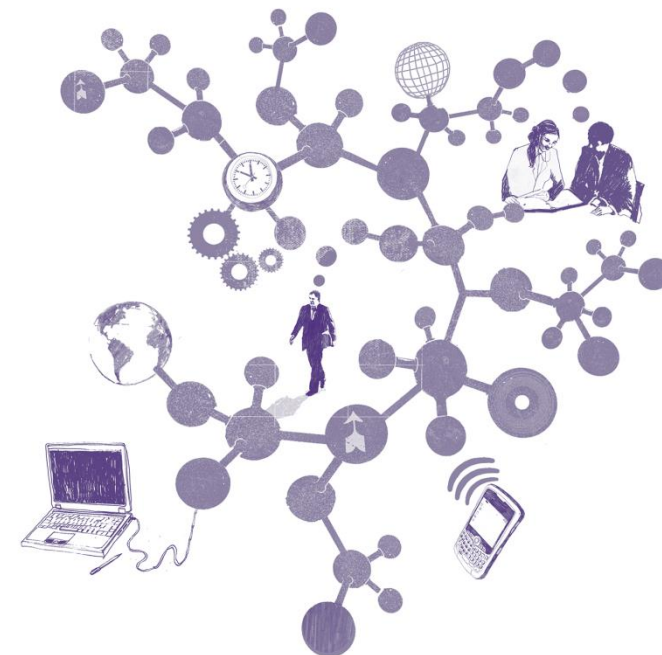
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Executive summary

Purpose of this letter

Our Annual Audit Letter (Letter) summarises the key findings arising from the work that we have carried out at Warwickshire County Council (the Council) for the year ended 31 March 2016.

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

We reported the detailed findings from our audit work to the Council's Audit and Standards Committee as those charged with governance in our Audit Findings Report on 8 September 2016.

Our responsibilities

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

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

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

Our work

Financial statements opinion

We gave unqualified opinions on the Council's financial statements, which include the Pension Fund financial statements, on 23 September 2016. We issued our report confirming the pension fund financial statements were consistent with those in the Pension Fund Annual Report on 6 October 2016.

Value for Money Conclusion

We were satisfied that the Council put in place proper arrangements to ensure economy, efficiency and effectiveness in its use of resources during the year ended 31 March 2016. We reflected this in our audit opinion on 23 September 2016.

Whole of Government Accounts

We completed work on the Council's consolidation return following guidance issued by the NAO and issued an unqualified report on 13 October 2016.

Other Statutory Powers

We have not identified any issues that have required us to apply our statutory powers and duties under the Act in 2015/16.

Certificate

We are currently unable to certify that we have completed the audit of the accounts of Warwickshire County Council as we have not yet completed the work in respect of objections received.

Other work completed

During 2015/16 we have continued to support the Council in a number of other areas, including certification of the Teachers Pension return and provision of our CFO Insights service.

Working with the Council

During 2015/16 we have worked with the Council in a number of areas:

An efficient audit – in partnership with the Council's finance team the bulk of our audit work was completed by the end of July 2016 as the Council moves towards the earlier closedown requirements for 2017/18. We will look to make further progress in 2016/17 and work with the Audit and Standards Committee to look at opportunities for bringing forward the date of reporting our audit findings.

Understanding your operational health – through the value for money conclusion we provided you with assurance on your operational effectiveness. We are aware that the final confirmation of the Council's settlement announced in the 2015 autumn statement has required the Council to identify around a further £67 million worth of savings over the next 3 years. In September 2016 the Council began a consultation on possible options which it aims to conclude in February 2017. The Council has a track record of sound financial management and working together to identify the best solutions for the people of Warwickshire, even where this means difficult decisions need to be made. However, you have recognised that the scale of reductions now needed will require you to look for further innovative solutions and that the shape and size of the Council and service provision could look significantly different by 2020. We will continue to independently review and report upon the Council's arrangements and progress in this period and provide both support and challenge where required.

Sharing our insight – through regular updates to officers and the Audit and Standards Committee. For 2016/17 one of the key areas we will provide support on is the new accounting requirements for Highways Network Assets.

Supporting development – sharing publications on areas such as Building a Successful Joint Venture

Providing information – with access to CFO insights, our online analysis tool providing you with access to insight on the financial performance, socio-economy context and service outcomes of councils across the country.

Further details are set out on page 12

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

Grant Thornton UK LLP
October 2016

Audit of the accounts

Our audit approach

Materiality

In our audit of the Council's accounts, 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 our audit of the Council accounts to be £13,907,000, which is 1.8% of the Council's gross revenue expenditure. We used this benchmark, as in our view, users of the Council's accounts are most interested in how it has spent the income it has raised from taxation and grants during the year.

We also set a lower level of specific materiality for certain areas such as cash, senior officer remuneration and external audit fees.

We set a lower threshold of £695,000, above which we reported errors to the Audit and Standards Committee in our Audit Findings Report.

Pension Fund

For the audit of the Warwickshire Pension Fund accounts, we determined materiality to be £16,381,000, which is 1% of the Fund's net assets. We used this benchmark, as in our view, users of the Pension Fund accounts are most interested in the value of assets available to fund pension benefits.

We set a lower level of specific materiality for certain areas such as management expenses and related party transactions. We set a threshold of £818,000 above which we reported errors to the Audit and Standards Committee.

The scope of our audit

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

This includes assessing whether:

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

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

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

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

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

Audit of the accounts – Warwickshire County Council

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

Risks identified in our audit plan	How we responded to the risk
<p>Valuation of surplus assets and investment property and fair value disclosures under IFRS 13</p> <p>The Council changed the basis on which it valued surplus assets and investment property in 2015/16 because of the introduction of a new international financial reporting standard (IFRS 13). Investment properties represent 2.5% of the Council total assets and their value is estimated by property valuation experts.</p> <p>The Council also needed to make changes to the disclosures for items valued at fair value under the new financial reporting standard.</p>	<p>As part of our audit work we:</p> <ul style="list-style-type: none"> • Reviewed whether the experts used by the Council were sufficiently knowledgeable and independent for us to rely on their work • Reviewed the Council's instructions to its valuer and the information on the assets it gave to them • Reviewed the valuer's report to understand the valuation method used and any key assumptions.. • Tested revaluations made during the year to ensure they were input correctly into the Council's asset register • Reviewed the disclosures made by the Council in its accounts to ensure they met the requirements of IFRS13 and of the CIPFA Code of Practice. <p>We did not identify any material issues to report in relation to this risk.</p>
<p>Valuation of property plant and equipment</p> <p>The Council's property, plant and equipment, including its housing stock, represents 81% of its total assets. Their value is estimated by property valuation experts.</p> <p>The Council revalues these assets on a rolling basis.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • Reviewed whether the experts used by the Council were sufficiently knowledgeable and independent for us to rely on their work • Reviewed the Council's instructions to its valuer and the information on the assets it gave to them • Reviewed the valuer's report to understand the valuation method used and any key assumptions. • Discussed with management the key assumptions they made about the basis of valuation, including asset lives, to ensure these were appropriate. • Checked that the valuation had been correctly reflected in the Council's asset register. <p>We did not identify any material issues to report in relation to this risk.</p>
<p>Valuation of pension fund net liability</p> <p>The Council's pension fund asset and liability, as reflected in its balance sheet, represents a significant estimate in the accounts and comprises 58% of its total liabilities.</p> <p>The values of the pension fund net liability is estimated by specialist actuaries.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • Documented and walked through the key controls put in place by the Council to ensure they were designed as expected. • Reviewed whether the experts used by the Council were sufficiently knowledgeable and independent for us to rely on their work • Reviewed the Council instructions to its actuary and tested the information on staff and pensioners it gave them to calculate the pension fund liability. • Reviewed the key assumptions made by the actuary using the work of an actuarial expert and tested whether any assumptions specific to the Council were appropriate. • Checked that the Council had correctly made entries in its accounts following the report from the actuary. <p>We did not identify any material issues to report in relation to this risk.</p>

Audit of the accounts – Pension Fund

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

Risks identified in our audit plan	How we responded to the risk
<p>Valuation of level 3 investments Level 3 investments are those where there is no existing market and the valuation depends on matters that are more subjective. These represent 9% of the value of the Pension Fund's total investments and their value is estimated by specialist valuers.</p>	<p>As part of our audit work we:</p> <ul style="list-style-type: none"> • Documented the controls in place to ensure that transactions were correctly recorded. • Tested a sample of investments to fund manager reports and gained an understanding of the method used by the fund manager to value these investments. • Reviewed whether the experts used by the Council were sufficiently knowledgeable and independent for us to rely on their work <p>We did not identify any material issues to report in relation to this risk.</p>
<p>Disinvestment from assets managed by Blackrock Investment Management. The pension fund is in the process of moving all the assets it currently holds with Blackrock to Legal and General Investment Management (LGIM), as part of a pooling of passive mandates with other local government pension funds. LGIM already acts as a fund manager for the pension fund. The value of the holding with Blackrock represented 17% of the fund's net assets as at 31 March 2015 and as such we consider this disinvestment to represent a significant non-routine transaction.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> • Gained an understanding of the transaction including a review of supporting documentation • Reviewed the reconciliation of information provided by the fund managers, the custodian and the pension fund's own records and sought explanations for variances • Reviewed the accounting entries in the financial statements to ensure that they are consistent with our understanding of the supporting documentation and with the requirements of the CIPFA Code of Practice. <p>We did not identify any material issues to report in relation to this risk.</p>

Audit of the accounts

Audit opinion

We gave an unqualified opinion on the Council's accounts, including the pension fund financial statements, on 23 September 2016, in advance of the 30 September 2016 national deadline.

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

In preparation for the earlier sign off deadline of 31 July which will apply for the sign off of your 2017/18 accounts, we sought to complete most of our audit work and issue our draft Audit Findings Report by the end of July 2016. We are pleased to report that, by working closely with the Council's finance staff throughout the year, we were able to achieve this.

Issues arising from the audit of the accounts

We reported the key issues from our audit of the accounts of the Council to the Audit and Standards Committee on 8 September 2016. We identified no adjustments affecting the Council's reported financial position as a result of the audit process and agreed a number of presentational amendments to the draft accounts which were actioned by the Council.

Pension fund accounts

We also reported the key issues from our audit of accounts of the Pension Fund hosted by the Council to the Audit and Standards Committee on 8 September 2016. In addition to the key audit risks reported above, we made a number of recommendations for future action in relation to review of the format and content of the accounts in line with CIPFA guidance, assurance from Internal Audit on the activities of the Pension Fund and validation and challenge on information provided by experts used external experts when producing the financial statements.

Annual Governance Statement and Narrative Report

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

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

Whole of Government Accounts (WGA)

We carried out work on the Council's consolidation schedule in line with instructions provided by the NAO. We issued a group assurance certificate which did not identify any issues for the group auditor to consider on 13 October 2016.

Pension Fund Annual Report

We carried out work in order that we could state to you that the pension fund financial statements in the pension fund annual report were consistent with the pension fund financial statements in the Council's Statement of Accounts in accordance with International Standard on Auditing 810, Engagements to Report on Summary Financial Statements. We issued our unqualified opinion on 6 October 2016.

Other statutory duties

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

At the time of issue of this letter we were considering our response to objections received in relation to the 2015/16 financial statements, but had not yet determined whether any exercise of formal statutory duties would be necessary.

Value for Money conclusion

Background

We carried out our review in accordance with the NAO Code of Audit Practice (the Code), following the guidance issued by the NAO in November 2015 which specified the criterion for auditors to evaluate:

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

Key findings

Our first step in carrying out our work was to perform a risk assessment and identify the key risks where we concentrated our work. The key risks we identified and the work we performed are set out on pages 10 and 11.

Overall VfM conclusion

We are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2016.

Value for Money

Risk identified	Work carried out	Findings and conclusions
<p>Sustainable resource deployment</p> <p>The Council has a "One Organisation plan 2014-2018" in place which identified the need to make significant savings (£92m). Our assessment in 2014/15 was that it was on track to deliver. However, the spending review announcement in December 2015 has led to further reductions in funding which has led the Council to identify the need to revisit this plan and reassess levels of savings required for 2016/17 and beyond.</p>	<p>Discuss key strategic challenges and the Council's proposed response</p> <p>Review of reports to members on:</p> <ul style="list-style-type: none"> • the outturn position for 2015/16 and the budget plans for 2016/17 and 2017/18 • the Council's progress in updating its medium term financial strategy . 	<p>The Council underspent against controllable budgets by £1.831m in 2015/16 and as at the end of 2015/16 remained on track to deliver the required savings as set out in the "One Organisational Plan 2014-18".</p> <p>In response to the December 2015 spending review the Council has launched a new 3 year "One Organisational Plan 2017-2020" aimed at identifying further savings by 2020 to enable continued delivery of a balanced financial position. A further update on progress was presented to the Council in September 2016 and consultation started on identifying an additional £67m of savings required by 2020.</p> <p>The Council approved a 2016/17 budget in February 2016 which includes:</p> <ul style="list-style-type: none"> • Savings requirements of £16.062m in 2016/17 and £20.236m in 2017/18 • Use of reserves and contingencies in 2016/17 of £21.546m.
<p>Working with partners and other third parties</p> <p>The West Midland Combined Authority (WMCA) has been set up within the region in order to help rebalance the West Midlands economy, closing the £16bn output gap and leading the Midlands Engine. In order to do this the WMCA needs to work together across geographic boundaries and sectors.</p> <p>In May 2016 the Council have taken the decision to join WMCA as a non-constituent member with a view to negotiating the basis of an acceptable deal on which Warwickshire could become a constituent member.</p>	<p>Discussion with officers and review of reports to members to assess progress made in development its membership of the West Midland Combined Authority and the extent to which it has been able to assess that this will support delivery of its strategic priorities.</p>	<p>WMCA was formally established as a new Authority on 17 June 2016. It has established a Leaders Board, which includes representation from Warwickshire County Council, and held its first AGM on 29 June 2016.</p> <p>The Leader of Warwickshire County Council is the Finance & Property Portfolio holder for the WMCA.</p> <p>The Council has started discussions on the terms of an agreement which could allow it become a constituent member and the role that it would play in the next phase of devolution negotiations.</p>

Value for Money

Risk identified	Work carried out	Findings and conclusions
<p>Working with partners and other third parties</p> <p>In March 2016, NHS England announced plans for area-based Sustainability and Transformation Plans (STPs) aimed at driving improvements in health and care outcomes between 2016 and 2021. One of the areas announced for these plans covers Coventry and Warwickshire.</p> <p>The Council will need to engage with other health and local government bodies within the Coventry and Warwickshire STP area to ensure robust plans are developed and delivered.</p>	<p>Discussion with officers and review of reports to members to assess progress on:</p> <ul style="list-style-type: none"> development and delivery of Sustainability and Transformation Plans for Coventry and Warwickshire <p>Discussion with officers and review of reports to members to assess progress on:</p> <ul style="list-style-type: none"> Implementation of the Better Care Fund 	<p>The Council's Interim Strategic Director, People Group is a member of the Sustainability and Transformation Board of the Coventry and Warwickshire STP, which has been formally meeting on a fortnightly basis since April 2016 and is also attended on a regular basis by the Council's Chief Executive. There is also a Programme Board which is attended by the Director of Public Health and the Head of Strategic Commissioning.</p> <p>The Coventry and Warwickshire Health and Well Being Boards agreed a joint concordat in June 2016 setting out how they will work together on common goals for the population.</p> <p>The STP have set out formal ambitions and plans in a June 2016 submission to NHS England, in line with the national timescales. These plans address all required areas set out in the national framework for STPs. Along with other areas nationally there is further work to be done during the autumn on the delivery plans.</p> <p>The Council has clear plans in place for the Better Care Fund:</p> <ul style="list-style-type: none"> total annual spend covered by agreed schemes - £36.1m Warwickshire County Council agreed contribution - £3.7m. <p>Detailed specifications have been agreed for all schemes included within the fund, setting out the purpose, aims, spending plans, commissioning and contracting arrangements for each scheme. Actual spend by scheme is monitored throughout the year.</p> <p>The Council has reviewed governance arrangements around the Better Care Fund and has taken action in 2015/16 to strengthen the support to the Health and Well Being Board through the establishment of a HWB Executive Team which includes chief officer representation from health and social care bodies across Warwickshire and allows strategic oversight of both the BCF and the STP.</p> <p>The Health and Well Being Board has agreed a range of metrics to monitor performance on health outcomes, including:</p> <ul style="list-style-type: none"> Non elective admissions Delayed transfers of care Residential admissions Reablement Carer reported quality of life Management of long term conditions. <p>Whilst targets set for 2015/16 in 4 of these 6 areas were not met, their use provides a clear focus on the outcomes which the Health and Well Being Board is seeking to achieve through the work of the Better Care Fund.</p>

Working with the Council

Our work with you in 2015/16

We are really pleased to have worked with you over the past year. We have established a positive and constructive relationship. Together we have delivered some great outcomes.

An efficient audit – we worked with you to complete the bulk of our 2015/16 audit work and issue our draft Audit Findings Report by the end of July 2016. Our audit team are knowledgeable and experienced in your financial accounts and systems. Our relationship with your team provides you with a financial statements audit that continues to finish ahead of schedule releasing your finance team for other important work.

Understanding your operational health – through the value for money conclusion we provided you with assurance on your operational effectiveness. We highlighted key risks in relation to the final challenges faced by the Council and effectiveness of partnership working, and discussed our assessment on these risks with your officers and the Audit and Standards Committee.

Sharing our insight – we provided regular updates to your officers and Audit and Standards Committee covering best practice. Areas we covered included Innovation in public financial management, Knowing the Ropes – Audit Committee Effectiveness Review, Making devolution work, and Reforging local government. We have also shared with you our insights on advanced closure of local authority accounts, in our publication "Transforming the financial reporting of local authority accounts" and will continue to provide you with our insights as you bring forward your production of your year-end accounts.

Supporting development – We have shared with you our publication on Building a Successful Joint Venture and are able to continue to support you as you consider greater use of alternative delivery models for your services.

Providing information – We provided you with access to CFO insights, our online analysis tool providing you with access to insight on the financial performance, socio-economy context and service outcomes of councils across the country.

Working with you in 2016/17 - Highways Network Asset

The Code of Practice on Local Authority Accounting (the Code) requires authorities to account for Highways Network Asset (HNA) at depreciated replacement cost (DRC) from 1 April 2016. The Code sets out the key principles but also requires compliance with the requirements of the recently published Code of Practice on the Highways Network Asset (the HNA Code), which defines the assets or components that will comprise the HNA. This includes roads, footways, structures such as bridges, street lighting, street furniture and associated land. These assets should always have been recognised within Infrastructure Assets.

The Code includes transitional arrangements for the change in asset classification and the basis of measurement from depreciated historic cost (DHC) to DRC under which these assets will be separated from other infrastructure assets, which will continue to be measured at DHC.

This is expected to have a significant impact on the Council's 2016/17 accounts, both in values and levels of disclosure, and may require considerable work to establish the opening inventory and condition of the HNA as at 1 April 2016.

Working with the Council continued

Under the current basis of accounting values will only have been recorded against individual assets or components acquired after the inception of capital accounting for infrastructure assets by local authorities. Authorities may therefore have to develop new accounting records to support the change in classification and valuation of the HNA.

The nature of these changes means that Finance officers will need to work closely with colleagues in the highways department and potentially also to engage other specialists to support this work.

Some of the calculations are likely to be complex and will involve the use of external models, a combination of national and locally generated rates and a number of significant estimates and assumptions.

We have been working with the Council on the accounting, financial reporting and audit assurance implications arising from these changes. We have issued two Client Briefings which we have shared with your finance officers. We will issue further briefings during the coming year to update the Council on key developments and emerging issues.

This significant accounting development is likely to be a significant risk for our 2016/17 audit, so we have already had some preliminary discussions with the Council to assess the progress it is making in this respect.

We have agreed that we will undertake early work with you in 2016/17 to review your progress and arrangements for dealing with the accounting for the HNA in your financial statements and provide early audit feedback.

We will continue to liaise closely with the senior finance team during 2016/17 on this important accounting development, with timely feedback on any emerging issues.

The audit risks associated with this new development and the work we plan to carry out to address them will be reflected in our 2016/17 audit plan.

We will also continue to work with you and support you over the next financial year. Locally our focus will be on:

- An efficient audit – continuing to deliver an efficient audit
- Understanding your operational health – we will focus our value for money conclusion work on your continued implementation of savings, and development of partnership arrangements.

Appendix A: Reports issued and fees

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

Fees

	2015/16 Planned fees £	2015/16 Actual fees £	2014/15 Actual fees £
Statutory audit of Council	94,539	94,539	126,052
Statutory audit of Pension Fund	23,892	23,892	23,892
Agreed fee variation - Pension Fund	1,328	1,328	1,328
Total fees (excluding VAT)	119,759	119,759	151,272

Fees for other services

Service	Fees £
Audit related services:	
• Certification of Teachers' Pension return	4,200
Non-audit services	
• CFO insights	30,000 (payment covers 3 year contract @ £10,000 per year)

Reports issued

Report	Date issued
Audit Plan – County Council	February 2016
Audit Plan – Pension Fund	February 2016
Audit Findings Report – County Council	August 2016
Audit Findings Report – Pension Fund	August 2016
Annual Audit Letter	October 2016



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