

# Audit Progress Report and Sector Update

Cumbria County Council and Cumbria Local Government Pension Scheme  
Year ending 31 March 2020

September 2020



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# Introduction

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This paper provides the Audit & Assurance Committee with a report on progress in delivering our responsibilities as your external auditors.

The paper also includes a summary of emerging national issues and developments that may be relevant to you as a local authority.

Members of the Audit & Assurance Committee can find further useful material on our website, where we have a section dedicated to our work in the public sector. Here you can download copies of our publications [www.grantthornton.co.uk](http://www.grantthornton.co.uk).

If you would like further information on any items in this briefing, or would like to register with Grant Thornton to receive regular email updates on issues that are of interest to you, please contact either your Partner or Engagement Managers.



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# Audit Deliverables

2019/20 Deliverables	Planned Date	Status- Council	Status-Scheme
<b>Audit Scope Letter 2019/20</b> Confirming audit fee for 2019/20. See separate agenda item for letter updated in August 2020, outlining our fee for the Scheme and Council audit's.	February 2020 August 20202	Complete Complete	Complete Complete
<b>Audit Plan</b> We are required to issue a detailed audit plan to the Audit and Assurance Committee setting out our proposed approach in order to give an opinion on the Council and Scheme's 2019-20 financial statements and a Conclusion on the Council's Value for Money arrangements.	September 2020 (Council) July 2020 (Scheme)	Complete	Complete
<b>Audit Findings Report</b> The Audit Findings Report will be reported to the November Audit and Assurance Committee.	November 2020	Not yet due	Not yet due (in draft)
<b>Auditors Report</b> This is the opinion on your financial statement, annual governance statement and value for money conclusion.	November 2020	Not yet due	Not yet due
<b>Annual Audit Letter</b> This letter communicates the key issues arising from our work.	December 2020	Not yet due	Not yet due

# FRC review of Grant Thornton's external audit of Cumbria County Council's 2018/19 financial statements and 2018/19 VfM Conclusion work

The FRC's Audit Quality Review team has completed its review of the 2018/19 external audit of the Council's financial statements and of the VfM Conclusion work undertaken by Grant Thornton. Their report sets out an assessment of the audit quality, key findings and scope of the review undertaken the FRC.

## Audit quality assessment

Area	Audit quality assessment
Financial Statements Audit	Improvements required
VfM Arrangements Conclusion	Limited improvements required

## Key findings

Valuation of Property, Plant and Equipment ('PPE')	The audit team performed insufficient procedures to conclude that the value of revalued and non-revalued specialised properties was free from material misstatement.
Fraud risk	The audit team performed insufficient testing of journals to address r the risk of fraud.

There were no key findings to report in relation to the VfM arrangements conclusion.

## Scope of the review

<b>SIGNIFICANT RISKS</b>	<ul style="list-style-type: none"><li>• Valuation of Property, Plant &amp; Equipment</li><li>• Valuation of the net pension liability</li><li>• Management override of controls – journal entry testing</li><li>• Value for Money arrangements – financial outturn and contract management</li></ul>
<b>OTHER AUDIT AREAS</b>	<ul style="list-style-type: none"><li>• Expenditure</li><li>• Borrowings including PFI liabilities</li><li>• Cash and short-term investments</li><li>• Audit planning</li><li>• Quality of communications with the Audit Committee<sup>3</sup></li><li>• Independence and ethical considerations</li><li>• Completion and audit quality control procedures</li></ul>
<b>AUDIT MATERIALITY</b>	£16.2 million

### Impact of the FRC's review on the audit opinion on the 2018/19 financial statements

The FRC's focus of its review is mainly on the valuation of PPE, where it considers that more work should be done in this area as it is a very large number, and subject to estimation and management judgement. Members will of course note that PPE values do not in any way impact on General Fund expenditure or impact Council Tax levels, as all adjustments are reversed out under statute. We consider that in 2018/19 we undertook significantly more work on this area than we had planned to do at the start of the audit, and more work than had been the practice previously within this and other firms. This year we have also engaged our own auditor expert valuer Wilkes, Head and Eve, to provide additional challenge of the work carried out by management's expert valuer. We believe this will address the points made by the FRC.

The remaining points raised in the review are more about our processes, and we set out how we are responding to each point in turn. None of the points raised by the FRC, in totality, impact on the soundness of the true and fair opinion issued on the 2018/19 financial statements.

## Key finding 1 – Valuation of Property, Plant and Equipment

**Issue** – The valuation of PPE is complex and requires judgements on significant assumptions and the use of asset specific source data. The external audit team should test and challenge key assumptions and source data, including corroboration of those used by management’s valuation expert, in order to conclude there are no material misstatements. The external audit team performed insufficient procedures to conclude that the value of revalued and non-revalued OLB was free from material misstatement.

**Our response and work performed** – Whilst we carried out a wide range of work in respect of PPE, undertaking significantly more work than we had initially planned to do at the start of the audit, and also more work than has been the practice previously within the firm, we acknowledge we should have undertaken some further specific work over the key assumptions in respect of other land and buildings. Specifically, as part of the 2019/20 audit, we will evidence the challenge we provide in greater detail and we have already engaged a specialist valuation firm to support our challenge of management’s external valuer. In respect of assets not valued in year, we will build additional testing into our review programme to assess the potential impact of assets not revalued on the financial statements, including for those instances where it appears assets may have been understated

## Key finding 2 – Fraud risk

**Issue** – Management override of controls is a fraud risk which requires appropriate procedures, including journal entry testing, to address the risk. A lack of appropriate audit procedures over higher risk journals increases the risk that a material misstatement within the financial statements would not have been identified by the external audit team. The external audit team failed to perform sufficient testing of journals to address the risk of fraud. In particular the external audit team did not: consider how such a low number of journals being tested provided sufficient audit evidence over the risk of fraud; explain why a journal would only be subject to testing if it triggered three separate risk characteristics; evidence the rationale for how risk characteristics were assigned a particular risk score; and evidence their review of the journals listing for postings by senior management.

**Our response and work performed** – We accept that scope exists to improve on the team’s judgement for each factor. At an engagement team level, we have already reflected on how we will refine the basis of scoring in our 2019/20 file.

## Other finding 1 – Audit of the net pension liabilities

**Issue** – The valuation of net pension liabilities is a significant estimate, impacted by a number of assumptions and judgements. Auditors should obtain sufficient evidence over the impact of all significant inputs and assumptions used in the valuation, consider the valuation methodology applied and appropriately conclude over any differences identified. The Cumbria County Council audit file was not complete in that the external audit team did not document a sufficient assessment or evaluation of the audit work over the valuation of the Level 3 pension scheme assets. Notwithstanding that the firm had direct access to the pension scheme audit file, the Council audit file should have included an assessment of the valuation methodologies applied to the pension scheme assets and of the sufficiency of the audit evidence obtained. Furthermore, given the higher materiality levels used by the pension fund auditor, it is unclear how the external audit team were able to conclude over the sufficiency of the testing performed. With regards Firefighters 2006 and 2015 Schemes assumptions, the external audit team should have; quantified the financial impact of the assumptions being outside the range; corroborated the duration of liabilities; and analysed the age profile of members and the life expectancy assumptions.

### Our response and work performed

As the Engagement Lead is the auditor of both the main financial statements and the Pension Scheme, and the work is completed at the same time, we propose to build an additional review into our detailed accounts procedures. As part of this we will complete a working paper, which evidences our detailed review of the work of the Pension Scheme auditor and whether this is sufficient evidence for the Council's opinion.

The engagement team will ensure adequate documentation on any Firefighters 2006 and 2015 Scheme assumptions outside the acceptable ranges is on the file to support their reasonableness and being in line with expectation.

## Other finding 2 – Value for Money ('VfM') – financial resilience

**Issue** – For significant risks covering arrangements in place over financial outturn and sustainability and cost improvement plans, the external audit team should perform sufficient procedures to assess both the achievability of performance and cost improvement plans. The external audit team should have performed additional procedures over the 2019/20 savings plan to assess whether the council had robust plans to manage and deliver this. For example, the team should have held meetings with key management responsible for delivering saving initiatives, reviewed the key planned savings of £15.3 million on adult care (including challenging the head of services) and reviewed the progress on delivering all savings.

**Our response and work performed** – We will build additional procedures into our 2019/20 VfM programme, to include further meetings with key management responsible for delivering savings, as well as review where appropriate of progress in delivering individual savings programmes.



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# Sector update

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Councils continue to try to achieve greater efficiency in the delivery of public services, whilst facing the challenges to address rising demand, ongoing budget pressures and social inequality.

Our sector update provides you with an up to date summary of emerging national issues and developments to support you. We cover areas which may have an impact on your organisation, the wider local government sector and the public sector as a whole. Links are provided to the detailed report/briefing to allow you to delve further and find out more.

Our public sector team at Grant Thornton also undertake research on service and technical issues. We will bring you the latest research publications in this update. We also include areas of potential interest to start conversations within the organisation and with audit committee members, as well as any accounting and regulatory updates.

- [Grant Thornton Publications](#)
- [Insights from local government sector specialists](#)
- [Reports of interest](#)
- [Accounting and regulatory updates](#)

More information can be found on our dedicated public sector and local government sections on the Grant Thornton website by clicking on the logos below:



Public Sector



Local  
government

# Covid-19 and Local Government

Public services have been at the forefront of the emergency response to the Coronavirus (Covid-19) including local government. Very few local government services have not been impacted by the Covid-19, and councils have also had to create new service lines as part of the emergency response, such as their work in identifying and supporting shielded and other vulnerable citizens, and to redeploy people to new roles and assets to new functions (for example closed leisure centres repurposed as temporary mortuaries and food banks).

Prior to Covid-19 local government has had to adapt to significant reductions in funding during the period of austerity. For example, spending on local services fell by 21% in real terms between 2009-10 and 2017-18. However, underlying this reduction are much larger reductions to some services expenditure. In broad terms, councils managed during austerity by significantly reducing spending on more discretionary services in order to protect statutory services to the most vulnerable people, particularly social care services. In addition, councils have had to place greater reliance on fees and charges income, and to be innovative in the generation of new income source, including a more commercial approach, a trend which is changing as authorities seek to balance social outcomes with financial sustainability.

Covid-19 has had a further significant impact on local government finances, which is the result of three main factors:

- increase in expenditure in managing the emergency response, such as purchase of PPE, provision of food and medical supplies to shielded citizens, and increased costs in relation to adult social care;
- lost income due to closed services, such as leisure centres, and the reduction in other sources of income from other sources, such as car parking, business rates and council tax; and
- the non-delivery of savings plans.

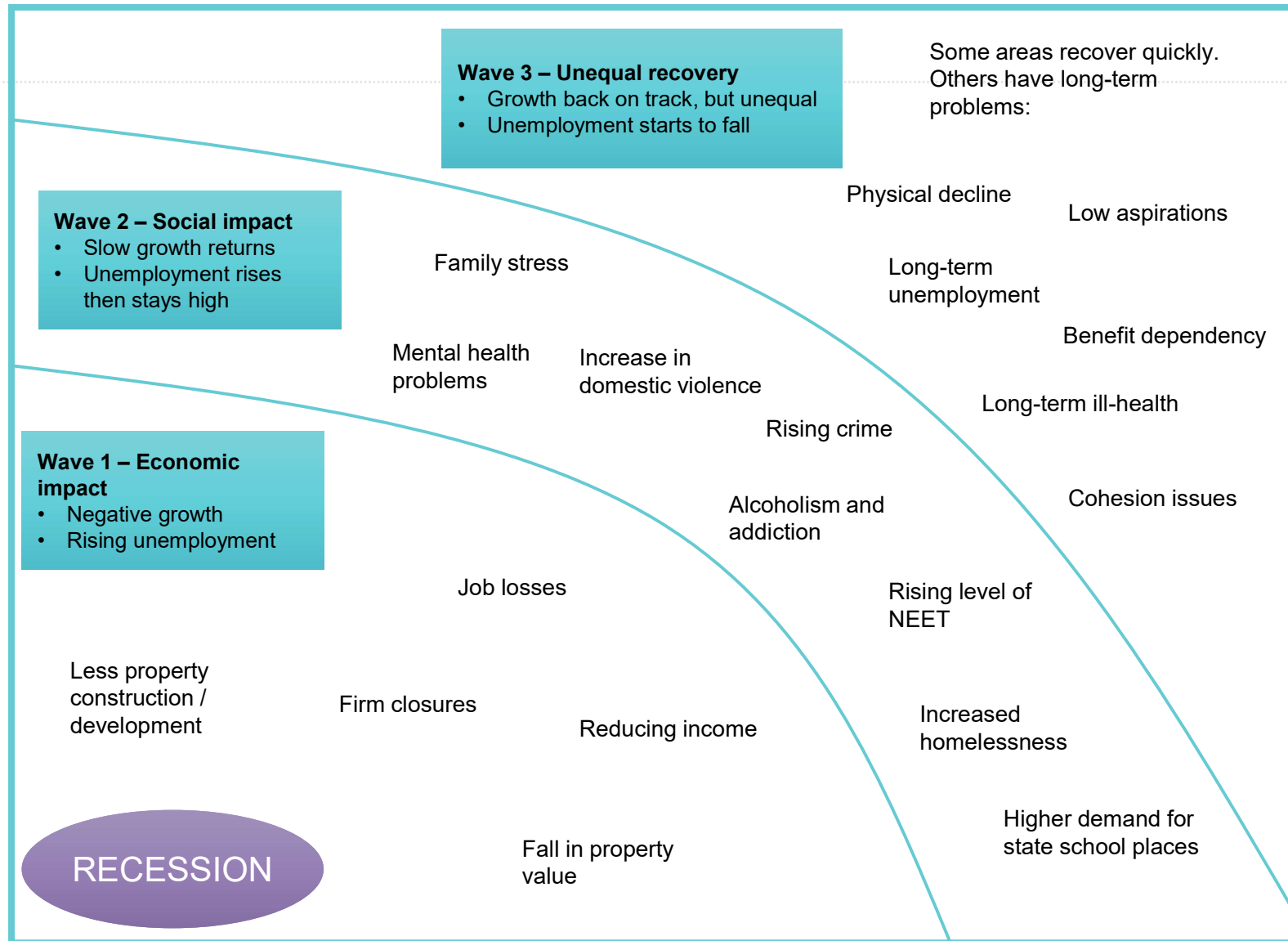
Whilst central government has made significant additional funding contributions to local government in recognition of the financial consequences of Covid-19, the total funding gap for councils in England is currently estimated to be £6billion by the LGA, with the sector still in the process of determining the longer term financial impact. The tranches of government funding provided so far have generally focussed on alleviating the financial pressures created by Covid-19 related spend, and so have had limited benefit for lost income such as that relating to leisure services.

This stark financial context has significant implications for the sector as councils start to move from the emergency response stage to the recovery planning stage of Covid-19. The key risks we will need to consider:

- how they stand up closed services such as leisure centres, the impact of Covid-19 on future demand, and the operational challenges of service delivery with on-going social distancing rules;
- how service delivery may need to change as a result of learning from Covid-19 and how long-lasting cultural and behavioural changes will impact on their operating models;
- the impact on local markets such as social care and transport, and the financial consequences of market and supply chain failure;
- how the economic impact of Covid-19 will impact on service need and on the demand for income generating services; and
- whether certain services will need to reduce or cease to manage the funding gap
- exploration of opportunities for more radical change that may have arisen from Covid-19, such as building on the large-scale transfer of care that has taken place and the opportunities regarding reablement, and broader integration with health.

Understanding the various scenarios, their financial implications, and the resources available to deliver them will be critical over the short to medium term.

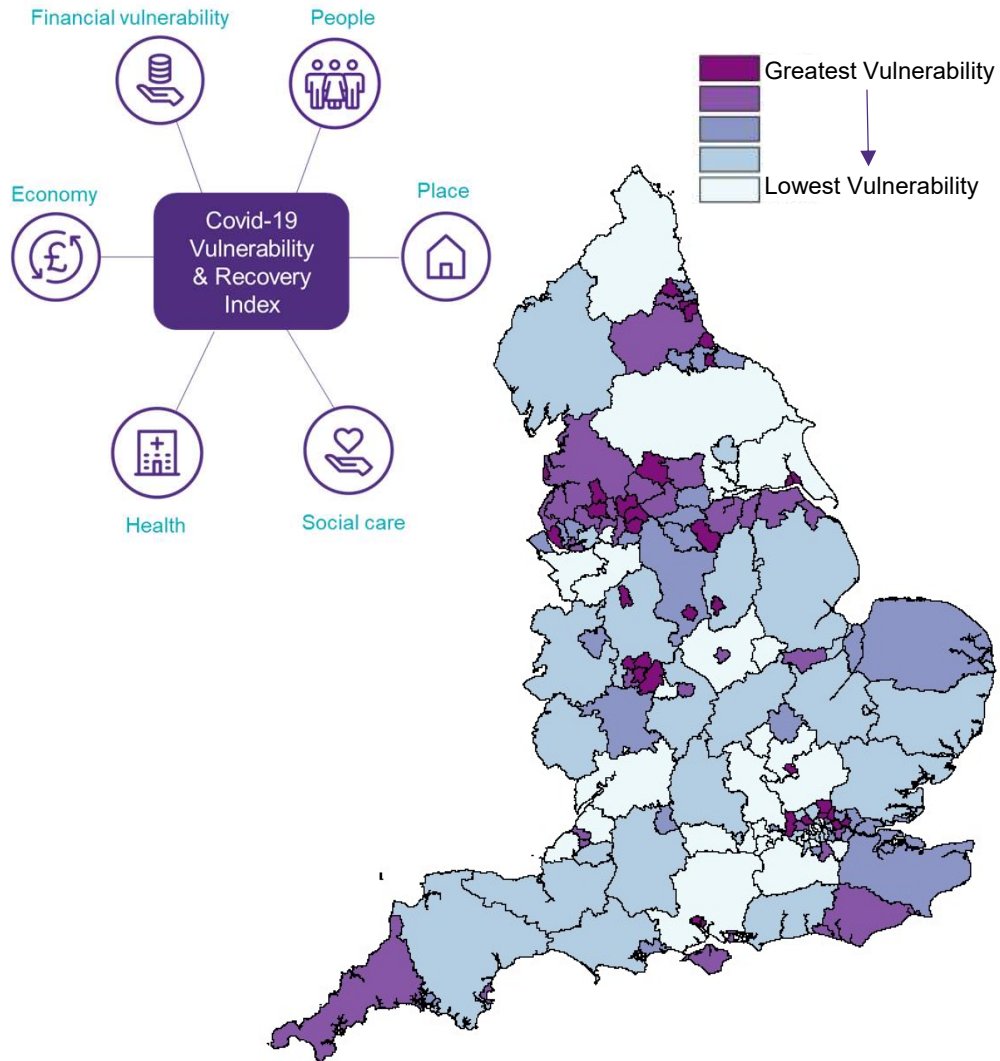
# Can we learn from previous recessions?



Source: Audit Commission







# Covid-19 Vulnerability Index

## Overall Index (including Financial Recovery basket)



# Scenarios and hypotheses

## Local authority areas in 12-24 months?

Theme	Reasonable worst case	Reasonable best case
<b>People &amp; community</b> 	<ul style="list-style-type: none"> <li>• Multiple lockdowns and ongoing disruption</li> <li>• Community dependency and expectation of sustained response</li> <li>• Turbulence and activism within the VCS</li> <li>• Socio-economic inequality is compounded</li> <li>• Failure of leisure and cultural services</li> </ul>	<ul style="list-style-type: none"> <li>• Smooth exit from lockdown to a “new normal”</li> <li>• Community mobilisation is channelled into ongoing resilience</li> <li>• Strengthened VCS relationships and focus</li> <li>• Systemic response to inequality is accelerated</li> <li>• Leisure and cultural services adapted to social distancing</li> </ul>
<b>Business &amp; economy</b> 	<ul style="list-style-type: none"> <li>• 16% reduction in GVA for 2020 based on OBR reference scenario</li> <li>• Slow / uneven economic recovery and “long tail” on unemployment</li> <li>• Central gov / BEIS focus investment on areas furthest behind</li> <li>• Loss of tourist &amp; student spend causes unmitigated damage</li> <li>• ‘V’ shaped recovery results in 2-3 year recovery period</li> </ul>	<ul style="list-style-type: none"> <li>• 5-10% reduction in GVA</li> <li>• Rapid economic recovery with employment levels close behind</li> <li>• Central government “back winners” with investment</li> <li>• Adaptation allows resumption of tourist and student economy</li> <li>• Business base is weighted towards growth sectors</li> </ul>
<b>Health &amp; wellbeing</b> 	<ul style="list-style-type: none"> <li>• Increased demand and escalating need due to fallout from lockdown</li> <li>• Newly-vulnerable cohorts place strain on the system</li> <li>• Unit costs increase further as markets deteriorate and providers fail</li> <li>• SEND transport unable to adapt to social distancing</li> <li>• Imposed disruption of care system</li> </ul>	<ul style="list-style-type: none"> <li>• Positive lifestyle changes and attitudes to care reduce demand</li> <li>• Needs of newly vulnerable cohorts met through new service models</li> <li>• New investment in prevention and market-shaping manage costs</li> <li>• New ways of working leading to stronger staff retention</li> <li>• Locally-led reform of health and care system</li> </ul>
<b>Political &amp; regulatory</b> 	<ul style="list-style-type: none"> <li>• Local government side-lined by a centralised national recovery effort</li> <li>• Unfunded burdens (e.g. enforcement and contact-tracing)</li> <li>• Councils in the firing line for mismanaging recovery</li> </ul>	<ul style="list-style-type: none"> <li>• Local government empowered as leaders of place-based recovery</li> <li>• Devolution and empowerment of localities</li> <li>• Councils at the forefront of civic and democratic renewal</li> </ul>
<b>Environment</b> 	<ul style="list-style-type: none"> <li>• Opportunity missed to capture and sustain environmental benefits</li> <li>• The end of the high street / town centres</li> <li>• Emissions and air quality worsened by avoidance of public transport</li> <li>• Capital programmes stuck</li> </ul>	<ul style="list-style-type: none"> <li>• Ability to invest in transport modal shift and green infrastructure</li> <li>• Changed working patterns rejuvenate town centres</li> <li>• Sustained impact on emissions due to new behaviours</li> <li>• New, shovel-ready infrastructure programmes</li> </ul>
<b>Organisational</b> 	<ul style="list-style-type: none"> <li>• Inadequate funding forces fiscal constraint</li> <li>• Working practices return to status quo – increased operating costs</li> <li>• Imposed structural change within the place</li> <li>• Austerity 2</li> <li>• Commercial portfolio becomes a liability</li> </ul>	<ul style="list-style-type: none"> <li>• Adequate funding enables a programme of targeted investment</li> <li>• Learning and adaptation to new operating environment</li> <li>• Energised system-wide collaboration and reform</li> <li>• Fiscal reform and civic renewal</li> <li>• Commercial portfolio reshaped for economic and social gain</li> </ul>

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# What strategy is needed in response?

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## *From response to recovery*

### **Learn, adapt and prioritise**

- Develop and test hypotheses around impact on place, services, operations, finances.
- Design rapid interventions - implement, test and evaluate.
- Learning from the response to lock in the good stuff – reflection on operations, services and the system.
- Set priorities and principles – what is the Council's purpose in an uncertain context and where will it focus?

## *Mitigating the worst case*

### **Consolidate and build resilience**

- Ensure that emergency management and response structures are resilient for the long haul.
- What is the minimum operating model to deliver this?
- Predict and model demand for social care and assess care market vulnerability.
- Contingency plans for structural disruption.
- Re-evaluate infrastructure pipeline.

## *Steering towards the best case*

### **Invest in renewal**

- Programme of priority-based investment framed by recovery and renewal.
- Focus on inequality, community resilience, targeted economic stimulus, skills and employment support and adapting public spaces.
- Continued system leadership, pushing for positive reform and resilience.

# Recovery planning and implementation

Set out below are examples of recovery planning activity that are being considered by councils. This activity needs to align to the Government's recovery strategy, and to existing government priorities such as levelling up, whilst future proofing against Covid-related government policy shifts.

Recovery planning	Recovery implementation
Recovery planning strategy and framework development.	Recovery plan implementation.
Risk assessments, research into which parts of the local economy have been most severely hit and which groups of people will need additional support.	Reviews of long term corporate plans/strategies, place vision, service plans, in context of phased lockdown release.
Planning for standing up closed services.	Place-based leadership – working with other public services, private and third sector to redefine place.
Integrating social distancing into the public realm, eg offering supplies of hand sanitiser and masks. Increased need for digital advertising and awareness raising.	Redefining front-line services, council as match-maker, convener and incentiviser as well as service deliverer or commissioner. Removal of internal silos (eg supporting vulnerable families).
Review of supply chain vulnerability.	More long-term and strategic partnerships and funding models for third sector.
Supporting local businesses evolve to a new normal post-COVID-19 world, including more trading on-line.	Re-evaluation of vulnerability, including eligibility criteria. Likely to put in place structures that outlast the crisis, such as provisions to help the homeless and those in gig economy jobs.
Providing leadership for longer-term investment and delivery, to support economic recovery rather than just focusing on short-term actions.	Review and update Local Plan.
Reframe capital programme to support economic, social and environmental recovery / sustainability	Reconfiguration of municipal estate and property portfolio and commercial investments.
Renewed strategic financial planning and focus on financial management.	Emergency planning reviews and learning.
Data recognised as core pillar of resilience, barriers to data collaboration and information governance removed/standardised	Long-term financial sustainability planning.
Government monitoring regime on additional funding for councils and Covid funding administered by councils.	Increase in outcomes based procurement and focus on social value.
Business cases for new investments or for Government.	Significant investment in digital capabilities – channel shift, remote working, etc.
HR capacity and welfare, building health and safety checks.	

