

# Annual Audit Letter

*Year ending 31 March 2018*

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London Borough of Sutton  
August 2018



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## Your key Grant Thornton team members are:

Engagement Lead

Ian Murray

T: 0207 7283 328

E: [Iain.G.Murray@uk.gt.com](mailto:Iain.G.Murray@uk.gt.com)

Senior Audit Manager

Paul Jacklin

T: 0207 7283 263

E: [Paul.J.Jacklin@uk.gt.com](mailto:Paul.J.Jacklin@uk.gt.com)

Assistant Manager

Keith Mungadzi

T: 0207 7282 393

E: [Keith.Mungadzi@uk.gt.com](mailto:Keith.Mungadzi@uk.gt.com)

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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 the London Borough of Sutton Council (the Council) and its subsidiaries (the group) for the year ended 31 March 2018.

This Letter is intended to provide a commentary on the results of our work to the Council/group and 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 and Auditor Guidance Note (AGN) 07 – 'Auditor Reporting'. We reported the detailed findings from our audit work to the Council's Audit and Governance Committee as those charged with governance in our Audit Findings Report on 26 July 2018.

## Our work

<b>Materiality</b>	We determined materiality for the audit of the groups financial statements to be £9,600,000, which is 2% of the group's gross revenue expenditure. We determined materiality for the audit of the pension fund accounts administered by the Council to be £6,416,000, which is 1% of the pension fund's net assets.
<b>Financial Statements opinion</b>	We gave an unqualified opinion on the Council/group's financial statements on 30 July 2018. We gave an unqualified opinion on the pension fund accounts of London Borough of Sutton Pension Fund 30 July 2018
<b>Whole of Government Accounts (WGA)</b>	We completed work on the Council's consolidation return following guidance issued by the NAO.
<b>Use of statutory powers</b>	We did not identify any matters which required us to exercise our additional statutory powers.

## 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 and group'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 and group's financial statements, we comply with International Standards on Auditing (UK) (ISAs) and other guidance issued by the NAO.

# Executive Summary

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<b>Value for Money arrangements</b>	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 report to the Council on 30 July 2018.
<b>Certification of Grants</b>	We also carry out work to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. Our work on this claim is not yet complete and will be finalised by 30 November 2018. We will report the results of this work to the Audit and Governance Committee in our Annual Certification Letter.
<b>Certificate</b>	We certify that we have completed the audit of the accounts of London Borough of Sutton in accordance with the requirements of the Code of Audit Practice.

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## Working with the Council

During the year we have delivered a number of successful outcomes with you:

- An efficient audit – we delivered an efficient audit with you in June/July, delivering the accounts before the early close deadline two months earlier than the previous year, releasing your finance team for other work. We working closely with your finance team to bring forward more work than previous years reducing the amount of work undertaken at the year end
- Sharing our insight – we provided regular audit committee updates covering best practice. We also shared our thought leadership reports
- Providing training – we provided your teams with training on financial accounts and annual reporting.

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**  
**August 2018**

# Audit of the Accounts

## Our audit approach

### Materiality

In our audit of the Council/group'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 group accounts to be £9,600,000, which is 2% of the group's gross revenue expenditure. We determined materiality for the audit of the Council's accounts to be £6,954,000, which is 2% of the Council's gross revenue expenditure. We used this benchmark as, in our view, users of the group and Council's financial statements are most interested in where the group and Council has spent its revenue in the year.

We set a lower threshold of £464,000, above which we reported errors to the Audit and Governance Committee in our Audit Findings Report.

### Pension Fund Materiality

For the audit of the London Borough of Sutton Pension Fund accounts, we determined materiality to be £6,416,000, 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 threshold of £321,000 above which we reported errors to the Audit and Governance Committee.

### 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 Statement of Accounts and the narrative report, annual governance statement and Annual Report published alongside the Statement of Accounts to check they are consistent with our understanding of the Council/group and with the financial statements included in the Statement of Accounts 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 is based on a thorough understanding of the Council/group'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

## 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><b>Going Concern</b></p> <p>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>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Reviewed the Council's Medium Term Financial Plan and savings programmes.</li> <li>• Reviewed the Council's outturn and reserves position.</li> <li>• Reviewed the Council's disclosure in the financial statements.</li> </ul>	<p>We are satisfied that the Council's financial statements are prepared on a going concern basis.</p>
<p><b>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 entities. We identified management override of controls as a risk requiring special audit consideration</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Reviewed the accounting estimates, judgments and decisions made by management.</li> <li>• Reviewed journal entry process and selection of large and unusual journal entries for testing back to supporting documentation.</li> <li>• Reviewed the accounting estimates, judgements and decisions made by management.</li> <li>• Reviewed unusual significant transactions.</li> </ul>	<p>Our audit work has not identified any evidence of management over-ride of controls.</p>

# Audit of the Accounts

## 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><b>Valuation of property, plant and equipment</b> The Council revalues its land and buildings on an rolling programme to ensure that carrying value is not materially different from current value. This represents a significant estimate by management in the financial statements.</p> <p>We identified the valuation of land and buildings revaluations and impairments as a risk requiring special audit consideration</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Reviewed management's processes and assumptions for the calculation of the estimate.</li> <li>• Reviewed the competence, expertise and objectivity of any management experts used.</li> <li>• Reviewed the instructions issued to valuation experts and the scope of their work.</li> <li>• Discussed with the Council's valuer the basis on which the valuation was carried out, challenging the key assumptions.</li> <li>• Reviewed and challenged the information used by the valuer to ensure it was robust and consistent with our understanding.</li> <li>• Tested revaluations made during the year to ensure they were input correctly into the Council's asset register.</li> <li>• Evaluated the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value.</li> </ul>	<p>Our audit work completed has not identified any significant issues in relation to the risk identified.</p>
<p><b>Valuation of pension fund net liability</b> The Council's pension fund asset and liability as reflected in its balance sheet represent a significant estimate in the financial statements.</p> <p>We identified the valuation of the pension fund net liability as a risk requiring special audit consideration.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Identified the controls put in place by management to ensure that the pension fund net liability is not materially misstated and assessed whether those controls were implemented as expected and whether they were sufficient to mitigate the risk of material misstatement.</li> <li>• Reviewed the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation.</li> <li>• Gained an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made.</li> <li>• Reviewed the consistency of the pension fund net liability disclosures in notes to the financial statements with the actuarial report from your actuary.</li> </ul>	<p>Our audit work has not identified any significant issues in relation to the risk identified</p>

# Audit of the Accounts Pension Fund

## 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><b>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 entities.</p> <p>We identified management override of controls as a risk requiring special audit consideration.</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Reviewed entity controls.</li> <li>• Reviewed accounting estimates, judgements and decisions made by management.</li> <li>• Reviewed unusual significant transactions.</li> </ul>	<p>Our audit work has not identified any evidence of management over-ride of controls.</p>
<p><b>The valuation of Level 3 investments is incorrect</b></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 identified the valuation of level 3 investments as a risk requiring special audit consideration</p>	<p>As part of our audit work we have:</p> <ul style="list-style-type: none"> <li>• Gained an understanding of the Fund's process for valuing level 3 investments and evaluated the design of the associated controls.</li> <li>• Reviewed the nature and basis of estimated values and consider what assurance management has over the year end valuations provided for these types of investment.</li> <li>• Considered the competence, expertise and objectivity of any management experts used.</li> <li>• Verified the investment balances to the fund manager and custodian report.</li> <li>• Tested the valuations by obtaining and reviewing the audited accounts, at the latest date for individual investments and agreeing these to the fund manager reports at that date. We reconciled those values to the values at 31 March 2018 with reference to known movements in the intervening period.</li> </ul>	<p>Our audit work has not identified any significant issues in relation to the risk identified</p>

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# Audit of the Accounts

## **Audit opinion**

We gave an unqualified opinion on the Council/group's financial statements on 30 July 2018, in advance of the national deadline.

## **Preparation of the accounts**

The Council/group presented us with draft accounts in accordance with the national deadline, 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.

## **Issues arising from the audit of the accounts**

We reported the key issues from our audit to the Council's Audit and Governance Committee on 26 July 2018.

We have not identified any adjustments to the financial statements that have impacted on the Council's financial position. Adjustments were classification and presentational.

## **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 within the Statement of Accounts 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.

## **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 29 August 2018.

## **Pension fund accounts**

We gave an unqualified opinion on the pension fund accounts of London Borough of Sutton on 30 July 2018.

We also reported the key issues from our audit of the pension fund accounts to the Council's Audit and Governance Committee on 30 July 2018. We did not identify any adjustments to the Funds financial position.

## **Certificate of closure of the audit**

We are also required to certify that we have completed the audit of the accounts of London Borough of Sutton in accordance with the requirements of the Code of Audit Practice.

# 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 key risks where we concentrated our work.

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

## 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 2018.

# Value for Money conclusion

## Key Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>The Council have historically managed their finances well. However, the financial environment is becoming even more challenging and at the time of preparing our audit plan the Council's anticipated 2017/18 outturn position was a net overspend of £2.5m</p>	<p>We responded to this risk by:</p> <ul style="list-style-type: none"> <li>• Review of budget monitoring reports and financial outturn reports to Members.</li> <li>• Discussion with senior officers</li> </ul>	<p>The Council continue to operate in an extremely challenging financial environment; 2017/18 was the seventh successive year of spending reductions. The council's financial position was closely monitored during the year. At the year end a small surplus of £0.160m was reported.</p> <p>The main areas of overspend during the year were:</p> <ul style="list-style-type: none"> <li>• £1.8m relating to Leaving Care Placement costs for young people still being looked after by the leaving care team. The number of young people has increased from 216 to 266. Also included in the balance is the additional costs of looking after 10 unaccompanied asylum seeking children who became 18 in the year.</li> <li>• £1.8m relating to Special Educational Needs transport. The number of students requiring Special Educational need transport has increased from 559 to 651 in the year. The cost is impacted by the number of Education, Health Care Plans that need to be maintained.</li> <li>• £600k relating to legal costs from a higher number of care proceedings and expert assessments needed than anticipated.</li> </ul> <p>Whilst additional budgetary growth had been allocated to these areas as part of the 2017/18 budget process, further financial pressure materialised, reflecting the inherent risks in these services. The Council are not alone in that 75% of Local Authorities have overspent their Children's Social Care budget which is closely linked to a 50% increase in looked after children nationally over the last four years.</p> <p>These overspends were offset by underspends within Environment, Housing and Regeneration and non service revenue accounts mainly due to net underspends on interest payable / receivable and the outcome of a review into the Council's approach to providing for debt repayments which resulted in a reduction to the level of annual contribution (MRP) saving of £1.5m, unspent contingency against Business Rates Revaluation and Apprentice Levy of £0.3m and a contribution from insurance reserve of £0.6m held in non-service budgets.</p> <p>The £10m of savings required for 2017/18 were deducted from budgets and the in year monitoring focussed on reviewing actuals against budget. The savings plans were not subject to separate monitoring, as monitoring was undertaken on overall budgets. In our view, this results in a lack of transparency and clarity in identifying whether the overspends are the result of under-delivery of savings plans or genuine unavoidable pressures from demand increases. Without this clarity, the Council are not properly able to assess the robustness of future plans and make an informed judgement as to the deliverability of the £8m of savings in the 2018/19 budget. The Council is currently implementing a methodology that will enable savings plans to be separately monitored for the remainder of the 2018/19 financial year. This is a positive move forward.</p> <p>The general fund balance is held to mitigate against risks such as unforeseen increased demand and cost pressures. The £0.160m underspend brings the general fund balance to £12.7m as at 31 March 2018 this includes £3.6m relating to schools. The General Fund position excluding schools of £9.1m represents 6.4% of the net revenue budget for 2018/19, above the 5% level set out in your reserves strategy.</p>

# Value for Money conclusion

## Key Value for Money Risks

Risks identified in our audit plan	How we responded to the risk	Findings and conclusions
<p>At the time of the plan the Council have set a balanced budget for 2018/19. The medium term financial strategy outlined the need to achieve further savings £5.8m by 2019/20. The projected funding gap is £2.2m in 2018/19 and expected to rise to £11.5m by 2020/21. The Council plan to utilise £2m of the reserves in 2018/19 to assist in balancing the budget</p>	<p>We responded to this risk by:</p> <ul style="list-style-type: none"> <li>• Review your progress in updating your medium term financial plan.</li> <li>• Review the savings plans for 2018/19 and 2019/20</li> </ul>	<p>2018/19 year will be particularly challenging year for the Council. In broad terms the reduction of Revenue Support Grant and continued reduction of government funding in 2018/19 £4m (8%) plus inflation and other costs of £3.6m and service growth cost pressures of £8.1m (including children’s safeguarding and adult social care) creates a significant budget gap before mitigation of £15.7m.</p> <p>This gap is addressed by the increase in Council Tax of 1.99% precept for adult social care at 2% raising total of £3.6, use of Integrated Better Care Funds and other monies £3.3m and £0.7m from the London Business rates Pool and delivery of £8.1m savings. Successful delivery of the budget and the medium term financial strategy will be dependent upon the effective continued management of demands across all council services and particularly in Children’s Services, and the continued development of robust of budgetary control and management of pressures in year.</p> <p>In 2018/19 you have assumed £8.1m of growth which includes £2.9m for Adult Social Care, £2.3m for Special Educational Needs transport costs and £750k in respect of implementing duties required by the Homelessness Reduction Act 2017. These were areas of increased demand in 2017/18. There remains some uncertainty about whether this level of growth will be sufficient to enable services to remain within budget for 2018/19.</p> <p>The Council’s savings plans for 2018/19 have been Red Amber Green (RAG) rated with £2.5m being Green, £5.8m Amber and £175k Red rated. Only £3.1m are new savings with the remainder being brought through from previous years. The significant areas of expected savings are Adult Social Care and Children’s safeguarding transformation schemes that are anticipated on delivering £3.5m savings and the reduction of Special Educational Needs transport costs £772k and the continued savings being brought about through waste collection service</p> <p>The council will need to monitor closely progress of these savings and the benefits anticipated from growth and investment in these key demand led services and ensure transformational schemes are implemented across the board.</p> <p>From 2019/20, the Council’s recommended approach to identifying and delivering savings is largely through an Outcomes Based Commissioning approach. Further work needs to be completed on the detailed allocation of savings to the themes. The move from Directorate based savings targets and plans to outcomes based savings targets and plans will require a different approach to the agreement, tracking and oversight of savings. This will mean a revised approach to the financial planning process and how budgets are allocated and then monitored.</p> <p>The Medium Term Financial Plan includes a gap of £3.6m in 2019/20 increasing to £8.7m in 2020/21 and then to £6.7m in 2021/22 and a further £5.4m in 2022/23. The forecast therefore, although with significant level of uncertainty, is that to balance the budget to 2022/23 savings of £24.5m will be required.</p>

# A. Reports issued and fees

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

## Reports issued

Report	Date issued
Audit Plan	29 March 2018
Audit Findings Report	26 July 2018
Annual Audit Letter	August 2018

## Fees

	Planned £	Actual fees £	2016/17 fees £
Statutory Council/group audit	94,290	94,290	94,290
Audit of Pension Fund	21,000	21,000	21,000
Audit of Sutton Housing Partnership subsidiary	33,000	33,000	38,000
Housing Benefit Grant Certification	12,300	TBC	15,068
<b>Total fees</b>	<b>160,590</b>	<b>TBC</b>	<b>168,358</b>

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA) Our fees for grant certification cover only housing benefit subsidy certification, which falls under the remit of Public Sector Audit Appointments Limited. Fees in respect of other grant work, such as reasonable assurance reports, are shown under 'Fees for other services'.

## Fees for non-audit services

Service	Fees £
<b>Audit related services</b>	
- Teachers Pensions Claim	6,000
- Pooling of Capital Receipts Return	2,800

## 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/group. The table above summarises all non-audit services which were identified.
- We have considered whether non-audit services might be perceived as a threat to our independence as the Council/group's auditor and have ensured that appropriate safeguards are put in place.

The above non-audit services are consistent with the Council/group's policy on the allotment of non-audit work to your auditor.



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